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- A New Deal under the Chandler Act
- Application of Depreciation Theory
- The Small-Town Hotel
- Capitalization
- Insurance Companies Look at Appraisals
- Depreciation and Obsolescence in Theatres
- Professional Ethics
- What the Attorney Expects of the Appraiser

AMERICAN INSTITUTE OF REAL ESTATE APPRAISERS

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The APPRAISAL JOURNAL

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WE CHANGE OUR NAME

APRIL is a happy month. It brings with it a real awakening of growing things. It brings new life, new ideas, new enthusiasms. And so, with this April issue, we announce

THE APPRAISAL JOURNAL

as the new and officially adopted name of this publication. The change is not the result of a sudden decision. Rather, it has been thrust upon us by the members and other readers who so refer to our Institute's quarterly magazine. The new title has the advantage of brevity and clarity and should leave no doubt as to the magazine's character and function.

No change is contemplated other than in the name itself. THE APPRAISAL JOURNAL will continue as a truly professional publication, devoted to feature articles and discussions of valuation and appraisal matters, and particularly their application to real estate. It will continue to offer its pages as a medium for the expression of informal opinions on controversial subjects, whether or not the particular contributor's views agree with those of the editors or of the majority of the Institute's members. The criteria in accepting manuscripts for publication will continue to be: first, that the subject be pertinent to the field of endeavor and, secondly, that the material be well prepared and presented.

We ask your indulgence in our efforts to cover such a constantly widening and sometimes turbulent professional movement, and we welcome at all times your criticisms and suggestions.

KILLING THE GOOSE

IN his regular financial column of February 16 (International News Service), M. S. Rukeyser presents an interesting discussion of the effect of the existing inheritance tax laws upon the national wealth. Of the predicament of those in the higher brackets, he says:

> "Top bracket inheritance taxes are radically changing the American system of passing on and conserving wealth.
>
> "The process in effect involves requiring heirs to repurchase the property for cash at about three-fourths of the assessed valuation.
>
> "This virtually means that persons at or near the top brackets are the mere custodians of property for the government, which owns the underlying lien."

Mr. Rukeyser goes on to show that where the estates are largely comprised of production goods, such as "factories, tools, and power equipment," the economic consequences must inevitably prove to be grave in a social sense. Obviously, to meet a 75 per cent tax on an estate represented principally in industrial plant property and facilities, the heirs are in no position to assemble the cash or its equivalent without seriously jeopardizing their business. And yet they are asked to do just that thing. This is rapidly bringing about a loss of initiative and an unwillingness to continue to expand and gamble on the uncertain business future that industry faces under the current economic conditions.

The result? Production curtailment; plant abandonment; and conservation of resources by the wealthy individual who is reaching the end of his career. This he

must do if he is to bring his estate to the liquid position essential for his heirs to meet the inheritance taxes. As we view it, if it were simply a matter of redistributing the wealth, it would not be so bad—just following the policy of "soak the rich," which has been attaining such popularity. But it is far worse than that. The curtailment of industrial progress is simply the forerunner of the cessation of individual progress. Fewer jobs — hence less income to labor, with the consequent reduction in purchasing power — and the entire economic and social structure is further undermined.

Mr. Rukeyser introduces statistics compiled by Reuben A. Lewis, Jr., of the Metropolitan Trust Company of Chicago, showing that more than 500 million dollars were paid by individuals in 1938 for the right to pass on their property to beneficiaries. Of this amount the Federal government took 382 million dollars, or 100 million dollars more than were ever collected before in one year. In these days of big figures a half billion dollars may not sound like important money, but think what a Henry Ford could do with it! In a happier day he would have plowed it back into production goods to make jobs for more men, more wages, increased purchasing power, and, finally, social advancement. Today, the funds in the hands of the government are static and, at best, may be looked upon as a further contribution to the "dole." And, do not forget, the plants which created this wealth are lying stagnant and facing disintegration, not so much from an actual lack of capital—there is plenty of it—but from the stifling of individual initiative.

The appraiser of industrial property sees the results on every hand — abandoned factories, smokeless chimneys, rusting railroad trackage. The appraiser of estates for inheritance taxes quickly senses the reasons. The values, and hence the taxes, are reduced — but at what a price!

Truly, we are "killing the goose that laid the golden egg" of opportunity, of economic and social progress, in this country. And what are we getting for the carcass? Just that — a carcass, with all of the feathers and most of the flesh gone!

●

HAVE YOU STOPPED STUDYING?

THE field of economic and social forces which touch upon the valuation of real property is so wide and of such a varied nature that any man who today assumes the title or sets himself up to be an appraiser, and upon whose opinion real estate is bought, sold, or mortgaged, immediately takes upon his shoulders a tremendous burden. This burden is the duty of keeping himself fully informed at all times regarding many things. Appraising, and the preparation of the mind and seasoning of the judgment of a good appraiser, must of necessity be a full-time job.

The whole economic pattern of world life today is so inextricably interwoven that a major disturbance of this pattern anywhere in the world quickly has its effect upon value in apparently entirely unrelated localities. Few people, unless they stop to think, realize the effect of Japan's undeclared war with China upon the value of the business, and indirectly of the plant and equipment, of every silk manufacturer in the world. Few people would say that the effect of the boycott of German goods by the Semitic elements of our population could or would affect a novelty manufacturer and a wholesaler dealing in toys and novelties — yet there has been such an effect.

The laboratory development of a new synthetic fiber has now materially affected values in whole communities in the United States: first, by the erection of new plants to manufacture this material: second, by the effect of the introduction of this material upon other communities where other types and kinds of fabrics are now being made.

Few professions call for such a wide study of the activities of the human race as appraising. Almost every bit of miscellaneous knowledge which a man can accumulate sooner or later is "grist in the mill" of the well-equipped appraiser's mind. The moment any man engaged in the appraisal of real estate ceases to read and to study and to evaluate in his own mind, and in terms of the value effect on his field of operations, all of the information available about economics, the political and social sciences, population, land use, construction, city planning, and myriads of other subjects, at that moment the worth of his opinion and accordingly his value to the profession and to his clients and employers begin to decline.

●

THE LONG TERM

FOR some years the saying, "Value is the present worth of future benefits arising from ownership," has been familiar to appraisers who are students of their vocation. This definition is satisfactory as far as it goes. It is all right as an abstract concept. However, it is incomplete as a rule to guide the appraiser in his practice. This is true because the benefits derivable from ownership from a given property can be worth different sums of money to different owners, and also because the benefits derivable from ownership can vary according to the time-basis (and other bases as well) upon which they are calculated.

One of the benefits accruing to an owner is the right to sell the property at the highest price obtainable from any purchaser, regardless of the purchaser's characteristics or his specific use-program for the subject property. The valúe of this right would be measured by the highest price currently obtainable from the prospective typical user, or from a specific user if one existed. To value the property upon the basis of this benefit, i.e., the highest price currently obtainable, would be proper if the appraiser's services are employed for the corresponding purpose. However, we are prone to distinguish between price obtainable, or price paid, and "value" and to justify the distinction by stating that a reasonable estimate of present worth of future benefits may not support the price currently obtainable or paid. If the distinction is warranted, it can be only upon the basis that the "future" benefits do not embrace the benefits of availing oneself of the price currently obtainable, but rather relate only to the benefits derivable through long-term use of the property or through holding it as a long-term investment.

Ordinarily, those who comprise by far the greatest portion of the users of appraisal services (typical prospective users and mortgage lending institutions) are desirous of knowing the appraiser's estimate of the present worth to typical users of the benefits which will be received by such users through long-term use and occupancy of the property or through holding it as a long-term investment and by following the highest and best program of utilization. Unless the short-term aspect of future benefits is eliminated, there is hardly any need to go beyond the estimation of the price obtainable in the market in the search for a reasonable value estimate.

Incidentally, failure to take full cognizance of the matters mentioned accounts for the arguments which sometimes prevail as to whether or not there can be only one value for any property at a given time. Plainly, values can be numerous for one property at one moment in time, but if you define the word to mean only one thing, and the definition is really successful in clearly limiting the significance of the term, then it is plausible to argue that there can be but one acceptable valuation for any one property.

However, there is no need to attempt to put the term into a strait jacket, and, in fact, the requirements of the business and economic structure prohibit such an attempt.

●

ROLLING THEIR OWN

IN the initial issue of *The Mortgage Banker*, January 1, 1939, Howell N. Tyson, Jr., makes a strong case for the appraisal by the banker himself, as opposed to that of the independent appraiser. We are asked to believe that the fellow who makes the loans ought to know best what the security is worth. Let's consider the idea for a moment.

The inveterate cigarette smoker is, or should be, a good judge of tobacco, and we are reliably informed that the dilettante can tell the difference in the various brands blindfolded. But give him a sack of "Bull Durham" and a pack of papers, and he is sunk, unless perchance he has acquired the necessary skill through an extracurricular college course or as a cowpuncher on an Arizona ranch. It's simply a matter of *knowing how!*

By the same token, it takes more than a knowledge of the principles of value to make a sound appraisal. Are we to believe that the mortgage bankers, as the "dealers" in appraisals, can "roll their own" by simply using the "makin's" saved up from former loan experiences? It doesn't make sense. Obviously, the data accumulated concerning property and property operation in the process of making loans are important and significant and may have a decided influence on particular valuation problems. However, the use and interpretation of these data in the light of many other circumstances that may influence the problem is the real job. The man who does it must know how.

Mr. Tyson really answers the question himself in the latter part of his article, wherein he stresses the great need for appraisal education among the members of his Association. As a possible means of accomplishing this, he suggests:

> "1. Set up a definite program of articles in the new association publication *The Mortgage Banker*, to be written by members of the Association or recognized appraisers; or establish a separate section of the publication to be devoted entirely to articles on and discussion of appraisal procedure and practice.
>
> "2. The organization of an appraisal school as a separate branch of the Association,—the course to be offered to members of the Association, their employees, or persons wishing to become members of the Association. The extent to which this might be carried to be determined by the number of people interested in the course and any requisitions set forth in possible future legislation affecting appraisal practice.
>
> "3. Conducting an appraisal clinic to be held either two or more days before the annual convention of the Association or as a separate part of and during the convention, or as a midseason activity. Such a clinic to lay particular stress on the opportunities for the instruction of young men."

Fine! Here, at least, we are in entire sympathy with the author. It is exactly

what the American Institute of Real Estate Appraisers has been concentrating upon for years. And, when the mortgage banker has trained himself as an appraiser, then — if he also acquires the necessary practical experience — he will be an appraiser. It is as simple as that. Mr. Tyson might have stated that many mortgage bankers have, during the past several years, availed themselves of the educational opportunities offered in the Real Estate Appraisal Courses sponsored and conducted by the Institute at The University of Chicago, Columbia University, and elsewhere. We are all for education, and anyone may enroll who has the rudimentary qualifications; he doesn't have to be an M.A.I. or even be engaged in real estate activities.

One thing, however, we believe Mr. Tyson has overlooked, and that is the question of the desirability of disinterested valuation. Has he forgotten the unfortunate experiences of the past when the reliance on "homemade" appraisals proved such a boomerang to financial interests? Errors might have been made, of course, by the independent appraisers— and frequently were. However, the criticism of disillusioned investors was far easier to bear if the banker could show that he had acted in good faith and in the most ethical manner. There was a real advantage in "passing the buck."

The prevailing trend is steadily toward the use of disinterested appraisals. Morally and ethically this is sound. It is a wise policy on the part of business and financial interests. There is more than a probability that it will become a legal necessity as evidenced by the gradual development of governmental regulations and restrictions in all matters of public finance. In any event, appraising is definitely taking its proper place as a distinct profession which is to render an increasing service to business and to the public at large. And the appraiser must *know how to make 'em!* It is a job in itself — not a side line.

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A NEW DEAL UNDER THE CHANDLER ACT

K. Lee Hyder, M.A.I.

BUSINESS today is about as happy as the orthodox stud poker player trained in an earlier era, the old-timer who wails, "This modern game of penny ante has just naturally ruined everything. What with 'Alaska,' 'spit-in-the-ocean,' 'one-eyed jacks wild,' and a hundred other illegitimate hybrids, to say nothing of a couple of extra cards, who knows what the hand is worth? And, if you do guess right, there's nothing in the pot anyhow." It is indeed a sad world.

Likewise, business, playing under changing rules, has been hard pressed to estimate the value of *its* "cards" during the past six years. Weird "hands" have emanated from the New Deal—"hands" that cause even the most hardened gambler to add up his few remaining chips and look nervously at his watch. But whatever else we may say, we must admit that the Amendment to the Bankruptcy Act, Section 77B, now superseded by the Chandler Act, looks like it had the makings of a "straight flush." It all rests on the "card in the hole," of course, but anyhow it is once again a case of mathematical probabilities and trained judgment.

What is the "card in the hole"? It is the set of circumstances underlying any going enterprise and its potentialities for future operation upon the assumed basis of its freedom from financial embarrassment. A business which is unsound economically cannot and will not long survive. If it is good, however, serves a useful purpose, and is competitively favorable, then it may stand a real chance — provided its debts are wholly or partially forgiven. It was to serve such inherently sound enterprises that the legislation was designed.

The purpose and intent of Section 77B was laudable enough and obviously twofold:

1. To speed up the machinery of reorganization for the conservation of assets and operating profits.
2. To save equities and the talent and knowledge of management, where justified.

The framers realized that all interests would be served best by continuing a business in operation, if possible, under those who knew it rather than by liquidating the assets (under bankruptcy) for the very doubtful benefit of first lien creditors. The talking points were excellent. The economic chaos just preceding the enactment of the Amendment had placed a large percentage of securities upon a market basis entirely inconsistent with and far below their probable real worth (*probable*, not *certain* — a point to be remembered). Bondholders in the mass were investors, not operators, and it looked as though they would be in the frame of mind to save a part of their investments even if they had to let the junior interests get a little cut in the process. Equity holders grabbed at the idea since they stood to salvage something from their all. The principle was evidently sound, constructive, and generally ac-

ceptable to informed interests of all types. That difficulties would arise in attempting to apply the law in actual practice to specific cases was inevitable, human nature being what it is.

All in all, however, this legislation has afforded many wavering business concerns and commercial properties a chance for rehabilitation, for resurrection. That it is lacking in far greater effectiveness is due primarily to a misconception of its practical application. There is the question of valuation, for example. After nearly five years of trial there still appears to be no adequate understanding of the part that fixed assets play in these most difficult problems. We hear a great deal about "transfer and sale of assets," "fair upset price," "value of respective interests," etc., etc., but little about the process or method of treatment or even the need for an underlying, interlocking valuation of the properties.

An appraisal is still viewed by many dealing with reorganization problems as a thing apart, a priced inventory of "brick and mortar" — informative, perhaps, but nonessential. If such were true, the contention might be a proper one. As a matter of fact, the "appraisal" for reorganization purposes is an estimate of future property demands and utilization. It is inextricably linked with all other phases of the investigation. This discussion is directed, therefore, particularly to the function of valuation in applying the legislation and the place the appraiser must take in its determination. Upon his efforts, in part at least, the "card in the hole" will be turned up — which may make the "hand" a winner.

FUNCTION OF VALUATION

The first step in the reorganization of an enterprise is a test of its solvency. In the final analysis, some person, court, or other agency must *declare* the value of all assets since the reconstructed balance sheet will be controlling. However, the book figures of fixed assets, reflecting the existing property, have no more significance than have the earnings of prior periods of operation carried on under differing circumstances — that is, as a practical guide to, but in no sense a measure of, futures. Nor can the figures be "picked out of a hat." They must be based upon a carefully developed analysis of demands, just as are all other elements involved in the program.

In the majority of cases the investment in fixed assets (land, buildings, and equipment) is by far the largest part of the total capital requirements in both an industrial and a commercial or real estate enterprise. Insolvency occurs only when the total liabilities are in excess of the total assets. Therefore, the value of the fixed assets is a major consideration in a test of business solvency. Since cost is not necessarily or usually a measure of value, and the book figures are frequently meaningless and can be accorded little weight, how then shall value be determined? And how indeed can a test of solvency, or the degree thereof, be determined for any proposed plan of reorganization unless the value of the fixed assets is fairly and properly estimated?

The answer to the last question is, of course, that it cannot. And yet the greatest number of reorganization programs under the Amendment to date have been presented to and adopted by the courts wherein value was a matter of simple declaration, voluntary agreement, or possibly left out entirely in favor of some arbitrary and patently unproven restatement of outstanding liabilities that had no factual support whatever.

With the adoption of the recent Chandler Act of 1938, this vicious practice may be overcome. This Act really is a general revision of the entire bankruptcy laws.

Chapter X of the Chandler Act now replaces former Section 77B of the Bankruptcy Act, which has been repealed. The Securities and Exchange Commission is brought into matters of reorganization for the first time, and while presumably its function is largely of an advisory nature, selected statements by the Commission are significant:

> ". . . . the most that can be expected is adequate machinery for the preservation of the assets of a corporation . . . . the realization of all the values that are in the enterprise . . . . and a fair and equitable allocation of these values among the several classes of security holders and claimants."

Even more encouraging are the remarks of one of the officials of the Commission:[1]

> "In order to test the fairness of a reorganization plan, it is first necessary to arrive at an estimate of the value of the property. The primary factor in arriving at this estimate is a capitalization of the 'reasonable prospective earnings' . . . . The question which this state of facts obviously presents is whether earnings themselves furnish a reliable basis of valuation . . . . that a reliable appraisal of physical properties must be had; and that these factors must be equated on a scientific basis to arrive at a figure as to value."

BASIS OF VALUE

Such statements on the part of the Securities and Exchange Commission lend hope for the future. Even though the Commission's function may be advisory only, its viewpoint must undoubtedly carry weight with the courts as well as with the parties to the reorganization.

This leads back to the question which still remains unanswered, "How then shall value be determined?" To the appraiser this raises many interesting problems; in fact, the very need for an answer constitutes a challenge to the entire appraisal profession.

To start with, the appraiser will insist that value is never *determined* — it is *estimated*. Agreed, in principle. However, it has already been brought out that value *must be determined* for such purposes. It may be by agreement or by the courts, but some person or agency must *fix* the value for the reorganized corporation. It should be fixed, of course, upon the basis of the most intelligent estimate possible; therefore, the appraiser may still be true to his principles in serving his particular function—and we may thus substitute properly the term *estimate* in discussing the basis of value.

Stripped to its fundamentals, the basis of reorganization must be the earnings outlook. Hence value must be estimated upon the expectancy of future net income from operation. To the real estate appraiser this sounds like old stuff. And isn't it? Well—yes and no. A valuation for reorganization purposes places a greater responsibility upon the appraiser, perhaps, than a valuation for any other purpose. It differs from a valuation for loan purposes, for instance, which might err on either side within moderate limits and still result in no great harm to anyone. For reorganization purposes, however, the appraiser's findings form the base for distributing equities. Once fixed, they are permanent, and an error of consequence is sure to hurt one or more of the various interests involved.

However, neither the purpose nor the degree of responsibility should influence the result. Real worth is contemplated, just as in any estimate of value, *with a certain indefinable but important exception.* The valuation is of necessity (arising as it does from the very need for such reorganization) almost entirely dependent upon estimates of futures under a change of operations which differ from those of the past, possibly in important and controlling particulars. The known results that form such an important guide to the valuation of a continuing going enterprise are practically nonexistent. New paths must be charted and frequently a different destination selected. Furthermore, the

[1] From an address by Abe Fortas, Assistant Director of the Public Utilities Division of the Securities and Exchange Commission, before a Legal Seminar in New York.

usual intent is to salvage management as fully as may be justified in order to preserve the highest possible value in the business as it now exists or as it may be revived. For these primary reasons the value should be estimated upon a basis of reasonable probabilities, and it may well be a far cry from the current market price for disposal to other interests.

This does not mean an *overvaluation*—not in any sense. It means that the value estimate should represent the amount at which a purchase would be *justified* rather than the sum which the assets or the securities might bring at open sale on the market (viewed in the light of the current impairment of the operating and financial condition of the enterprise). In a case in point the judge of a Federal District Court approved and commented upon the basis of value, as well as the appraiser's findings, as follows:

> "The court, after a consideration of the report of . . . . and the testimony taken upon hearing on exception thereto, is of the opinion that it is required to adopt the report, and find the fair market value of the properties of the Corporation to be . . . . This amount is less than the cost of replacement less depreciation. The reproduction cost was considered, as it should have been, by . . . . , but was not adopted as the market value. Under the conditions prevailing in the instant case the . . . . (appraiser) . . . . was correct in its rejection of the reproduction cost. The properties can be used for no other purpose than as . . . . As has been stated, no present market for the properties exists. *We are required to find an amount which would justify any person in purchasing them.* Such a purchaser would be interested in but two questions. The first, what income could be obtained from the properties; the second, the capitalized value of that income. No one would buy the properties at a greater sum than this capitalized value."
>
> (Italics, the author's.)

From the standpoint of the practical appraiser, this means that value must be estimated upon the basis of the highest use of the assets to the present interests, who, presumably knowing the properties and the business, would be enabled to get the best and quickest results from future operations. Under a concept of sale—the "fair upset price" to which we hear reference made—no different basis is contemplated. The appraiser would take this to mean a contemplated transfer to capital with equally competent and experienced management available to carry forward the future operations.

The latitude accorded to the determination of the value of the assets under various differing plans of reorganization is evident from the following quotations from Article X of Chapter X of the Chandler Act:

> "A plan of reorganization under this chapter . . . ."
>
> "(8) shall provide for any class of stockholders which is affected by the plan and does not accept the plan by the majority of the stock required under this chapter, adequate protection for the realization by them of the value of their equity, if any, in the property of the debtor dealt with by the plan, either, as provided in the plan or in the order confirming the plan, (a) by the sale of such property at not less than a fair upset price; or (b) by appraisal and payment in cash of the value of their stock; or (c) by such method as will, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection: Provided, however, That such protection shall not be required if the judge shall determine that the debtor is insolvent; . . . ."
>
> "(10) shall provide adequate means for the execution of the plan, which may include: the retention by the debtor of all or any part of its property; the sale or transfer of all or any part of its property to one or more other corporations theretofore organized or thereafter to be organized; the merger or consolidation of the debtor with one or more other corporations; the sale of all or any part of its property, either subject to or free from any lien, at not less than a fair upset price and the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein; . . . ."

It is seen from the above that the treatment accorded to the stockholders (equity capital) may be a major issue of valuation, not only of the entire property, but also of the respective classes of interests of creditors and/or stockholders if the debtor be found *not* insolvent. On the other hand, if insolvency is found, then the plan *may* include "the retention by the debtor of all or any part of its property." This means, in effect, that a plan is ac-

ceptable which appears to offer the best protection for the property's future, and, once determined, the respective interests may be "cut in" upon any reasonable basis. Usually this infers that the future rights of the respective interests are to be gauged very largely upon the character and extent of the *contribution which they will make financially or otherwise* to the reorganized corporation or property.

The appraiser may be called upon to estimate the value of all or of parts of the holdings or of the stock issued therefor. However, as previously brought out, the question of solvency or insolvency is paramount, and this calls for the initial valuation of the assets.

WHAT ARE FIXED ASSETS?

Fixed assets, as reflected upon the balance sheet of a corporation, may be, and frequently are, limited to the recorded investment in physical property—that is, land, building construction, and equipment. Goodwill or other intangibles, if entered at all, are usually and properly shown as a separate item. As considered in a valuation for reorganization purposes, however, fixed assets represent all property, tangible or intangible, that is existent and essential to future operations, excepting only current funds, materials and supplies, merchandise or product inventories, and other items of working capital. Investment items, of course, are assets, but placed in a different category.

The appraiser, therefore, in approaching the valuation of the property, and knowing that his valuation will be substituted for the book figures of "fixed assets" on the balance sheet as reconstructed, is undertaking to value the *property and attached business as a unit*—that is, to include the value which may properly inhere in the future in the possession of intangible assets. This does not mean that the appraised value will be something in excess of book values. On the contrary, it usually will be much less. But whatever it is, the estimate must recognize all elements that tend to create value upon a mobile rather than a static basis.

In the final reconstruction of the balance sheet other assets must also be appraised. The current items will usually be valued by the accountant. Inventories and investments must be analyzed and valued in accordance with their worth to the future going enterprise. In many instances the appraiser may include such items in his valuation, but they constitute separate and distinct problems in themselves.

NATURE OF PROPERTY CONTROLLING

The approach to the valuation will depend to a large extent upon the character of the property and business. An industrial enterprise, devoted to the manufacture, sale, and distribution of products or service, differs basically from the investment or income type of property. In the one instance, the facilities are merely the "tools" of the business and are to be considered separately at their "value for use"—for future use—to the reorganized enterprise. In the other, the property really constitutes the business itself since the product is nothing more than the *rental* of space to others. This distinction is evidenced in the very definition of the terms:[2]

> "*INDUSTRIAL PROPERTY* — In a broad sense — All the tangible and intangible assets pertinent to the conducting of an enterprise for the manufacturing, processing, and assembling of finished products from raw or fabricated materials. Also — in a limited sense — the land, fixed improvements, machinery, and all equipment (fixed or movable) comprising the facilities devoted to such enterprise."
>
> "*INVESTMENT PROPERTY* — The property which is within itself a business enterprise consisting of all tangible and intangible assets considered as integral with the property, assembled and developed as a single unit of utility for lease or rental (in whole or in part) to others for profit."

The limitations of this article prevent a full discussion of the subject of indus-

[2]Education and Research Committee, American Institute of Real Estate Appraisers, *Appraisal Terminology* (2nd ed.; Chicago, 1938), p. 43 and p. 46.

trial property evaluation. The process is complex in procedure although no different in fundamental principles. Perhaps the greatest difference is in the nature and sources of data required. In the industrial property the future prospects involve the study of many economic factors that may seem far removed from the specific property. These include the status and prospects of the basic industry; the availability of markets for products, which may depend upon many other lines of endeavor; competition in the same or substitute products; technological improvements in manufacturing processes and equipment; and the possible conversion of the properties to an entirely different character of business—to say nothing of labor relations, transportation problems, utilities' services, governmental restrictions, and many others. Any one of these factors may be progressing on an entirely different trend or rate of change than another, and yet all must be brought to the least common denominator in the process of making the value estimate.

In the valuation of the investment or income property there are also many complications, but the problem is nevertheless simplified to a considerable degree. The nature and sources of data are more localized, and the general economic conditions that affect the future value of the property are largely ironed out in the very data assembled. The intangible elements that may inhere in the holding are blanketed to a great extent in the direct estimation of the net income potentialities. The intangibles, however, are still present, and the weight that such intangibles represent in the property as a whole is of considerable importance in the estimates of risks, future continuity, and hence of final value.

For example, a department store, in the ordinary course of appraisal practice, may be considered as an income property—that is, it may be valued upon the basis of the capitalization of net income from rental. The reorganization of a department store, however, does not stop at this point. We are concerned here rather with the future prospects of the enterprise itself, and the real estate is only incidental although usually of the greatest significance. The appraiser's job is to estimate the worth of the fixed assets—all of them—in connection with the business of the future as a going concern. He may elect to set the real estate apart for consideration, although ultimately it will be but one phase of the whole. It must be remembered, however, that the securities held by the various interests constitute liens against both property and business earnings; furthermore, that bonds are issued upon the basis of real estate value, but are also secured by the net earnings from the business.

The same procedure followed in the case of a department store holds true in the case of a public garage, a theatre, or a hotel. Perhaps the valuation of a commercial hotel may be taken as a good illustration of the principles involved. The tangible property in a going hotel enterprise comprises the real estate (the land, improvements, and fixed equipment), the hotel furnishings and equipment (the furniture, carpets and draperies, kitchen and pantry equipment, linens, china, glass, and silver), and the essential working capital in food and other supplies and cash balance required to operate without financial embarrassment. The intangible property consists of the name and history of the hotel, established organization, and, in general, the goodwill of the local and traveling public. This leads to a natural segregation by the appraiser of the investment and assets, even though the entire enterprise is under one ownership, as follows:

Contribution by real estate: Land; improvements; fixed equipment.

Contribution by operating capital: Furniture and fixtures; working capital; knowledge, experience, and position in the hotel field.

When a hotel faced financial failure in the days prior to the Amendment to the Bankruptcy Act (Section 77B), there was very little to be done about it. The primary creditors and bondholders took over, and other interests were washed out. If the enterprise appeared to offer prospects for future operation, new capital was probably borrowed to the extent needed for rehabilitation, and the new owners went out to try and find a manager. Unfortunately, the new owners were primarily investors, not hotel operators. They knew nothing about a hotel or how to run it. Furthermore, a competent new manager was hard to get, and the former one was no doubt in ill repute due to the failure of the hotel, which might or might not have been the fault of the management.

Now, under the new legislation, an entirely different opportunity is afforded which may well be advantageous to all interests. As previously discussed, it is provided that the courts will consider various plans for reorganization and presumably approve the plan which appears to offer the best prospects for the future. The cards are reshuffled and redealt to the various interests, and in this case the equity owners are "dealt in" with everyone else. Of course the interests are considered in the order of their priority, but not necessarily in accordance with their prior financial relationship.

Returning to our analogy, it is now a question of two parts:

1. Does the "hole card" (the property and business prospects for the future) look good enough to warrant a continuance of the game?
2. How much does each player appear to contribute toward the success of the whole, upon the basis of which he will be "cut in" on the pot?

The appraiser is vitally concerned with the answer to the first question. His job is to supply the court with the material, or part of it, which will enable it to decide the question of bankruptcy. The answer to this question will indicate the further steps to be taken and the form that the proposed plans will assume. But the use of the appraisal does not stop here. The very data which the appraiser assembles and analyzes in his study of the valuation problem assist toward a solution of the second question.

It is not sufficient, therefore, that the appraiser render an opinion of value. Rather he must present, step by step, the factual information upon which he relied and the sources of such information, as well as the logic and reasoning which led him finally to his estimates and conclusions.

PLANNING THE APPRAISAL

A valuation of fixed assets for reorganization purposes requires perhaps a more complete and exacting preliminary study of the properties and business than for any other purpose. It goes far beyond a casual inspection of the property and neighborhood and the past history and results of operation. The appraiser, in effect, must formulate a *plan* of his own which he thinks would bring the property to its highest utility and earning power. He is concerned with the former financial structure only to the extent that it might have had a bearing upon the operating results of the past.

The appraiser is privileged to rely upon others for basic information if he so desires, whether this be regarding general questions of economics and business trends or specific matters such as statements of audit for prior years. But, in accepting such information assembled by others, he cannot adopt it in the sense he would follow usually in the valuation of a going profitable enterprise; he simply uses the information furnished by others to assist him in formulating a program for future property use which seems to offer the

greatest assurance of realization. The character and extent of assumed use may be a far cry from that which has prevailed in the past. It may be that his conclusions in that respect will be such as to exclude entirely as information the figures of actual past operation. In such event, he must hypothetically connect the property to whatever potential use appears the most likely to succeed. Then, upon a "when, as, and if" basis of approach, he estimates and considers future income, expense, and net profit. The cost of rehabilitating or converting the property to such change of use is, of course, to be deducted in estimating the present value.

In principle, the search for the highest and best use as a basis for valuation is no different than in a valuation for any other purpose. About the only departure is the degree of speculation involved in the appraisal for reorganization purposes. There may be several ways in which the enterprise could be adjusted to meet future conditions, any one of which might require a different form and degree of property utilization. If the appraiser is to fulfill his proper function to the extent of his responsibility, he must study every possibility and then lay down his plan or formula for valuation fairly and clearly and without prejudice or favor to any of the interests involved.

VALUATION PROCEDURE

With these fundamentals clearly in mind, let us see just how we may proceed with the valuation of the assets. Take the commercial hotel for illustration. What is the property worth? What is the "fair upset price" of the fixed assets—the physical properties and established business? That, in short, is the question presented for solution, the answer to which will in turn permit the reconstruction of the current balance sheet in order to determine solvency or insolvency of the enterprise.

Let us say that the preliminary survey and analysis of the property, its operations, and the economic conditions surrounding the enterprise have led to the general conclusion that there is a real need and place for the hotel in the community, that the building is well planned and constructed and compares favorably with competing hotels of a similar type. Then you may ask, "What is wrong with the hotel? Why is the company facing reorganization?"

The answer to these questions constitutes the first basic step in the appraiser's real study of the problem. One appraiser may make first a thorough survey of the property itself and then take up a detailed analysis of operations; another may reverse this approach. The order is not important perhaps, but both steps are essential. The appraiser may find that, while the hotel is modern, it is nevertheless out of balance in guest rooms, sample rooms, or public rooms; that the dining room facilities are out of date and require modernization; or that the furnishings and equipment are in poor condition and need many replacements in order that the rooms may be found attractive to guests.

Turning to the operations, his analysis may show initially that the fixed charges represented in interest on outstanding securities are entirely out of proportion to the occupancy and revenue, and hence that maintenance and replacements have been deferred in the attempt to maintain a sound financial position, which has led to a further reduction in occupancy and earnings and finally to financial disaster through failure to meet interest obligations.

For purposes of estimating the potentialities the appraiser then reconstructs the past operating statements by eliminating all interest and other financial expense—that is, he adopts the hypothesis that the property is owned in fee, and

thus develops just what the results of operation *would have been* upon such assumption.

The appraiser then turns to a consideration of futures. It is here that he accepts his greatest responsibility. In the almost certain absence of comparable sales of similar properties, he directs his investigation to an estimate of the *price which would be justified* at purchase—the "fair upset price." As previously suggested, however, *the value for continued utilization under competent management* may properly apply and not the current market price under forced sale, provided, of course, that the enterprise appears to warrant continuance.

The most logical procedure in valuing the real estate itself is to estimate the fair rental that capital (properly equipped and competent in hotel operation) could reasonably assume. This rental is then converted into capital value under rates of capitalization consistent with the character of the assets and the prevailing opportunities for equivalent investment returns. The estimating of such fair rental leads naturally into every phase of the hotel business. It has been brought out previously that the total value is contributed in part by real estate and in part by operating capital, both tangible and intangible.

The rental that the independent and prudent operator can afford to pay for the use of the real estate—land and improvements—will be the residue of net operating profits after he has satisfied the investment demands from operating capital—that is, furniture and fixtures and working capital—plus a satisfactory compensation for his contribution in the form of knowledge and experience in the hotel business. Obviously, the operator would not be interested in renting or purchasing the real estate simply for the privilege of obtaining a return upon his liquid capital. He would prefer to make other forms of investment attended with lower risks.

What rental can he afford to pay? To make this estimate the appraiser sets up a hypothetical operating statement for the future. Based upon his investigation he considers that the properties have been rehabilitated in such manner as to develop the maximum net income above all operating expense but before fixed charges. From this net income he deducts a fair return and a proper provision for depreciation upon the estimated investment in operating capital. The residue is then spread as between real estate and compensation to the intangible assets contributed by management. The amount assigned to real estate is the *fair rental*, which, in turn, may be processed into value just as in the case of any other income from real estate.

With the computation of real estate value once obtained, the estimated costs of rehabilitation essential to the realization of the net operating income are deducted, and the balance represents the value—the "fair upset price" which may be posted on the balance sheet in place of the book value of real estate.

This really is not as complicated as it sounds. The process does not differ in any material respect from that ordinarily adopted in any real estate valuation. The only essential difference arises from the more than usually difficult problems involved in projecting future operations and the necessity of breaking down the net income potentialities in accordance with the type and relative amounts of contributing capital.

In preparing the hypothetical operating statement, great care and sound judgment must be exercised, of course. A slight change in the estimated percentage of guest-room occupancy may have a great influence on anticipated profits. Expenses must be analyzed and estimated in the

light of *future* conditions—not those of the past. Maintenance and replacements must be predicated upon carefully prepared cost estimates and demands in building and building equipment. Furnishings and hotel equipment must be appraised at their "value for use" to the future enterprise, usually at the cost of reproduction new less depreciation of the used and useful property. This "value for use," after deducting therefrom any costs of rehabilitation, becomes the value to be posted on the balance sheet for furniture and fixtures in place of the book values for the same item.

Compensation for the contribution of management must be estimated with good judgment under all of the circumstances. Standards and precedents in the hotel field form the best guide to the appraiser. To a large extent the estimate differs little from the study of relative investment risks and demands in any income property. Sometimes this estimate may be set up upon a "fixed fee per guest room" basis; again, upon a "percentage of net operating profit." In instances where the margin of profit, even after relief from financial burdens, looks meager for the future, the compensation to the hotel operator would probably be set up as a fixed monthly or annual charge consistent with what an outside operator might expect to receive.

OTHER CHECKS AGAINST THE RENTAL ESTIMATE

In certain types of business the fair rental for the real estate may be subject to estimate, or at least to check upon the basis of ratios or percentages to sales volume. Most real estate appraisers are familiar with this method. For example, in the case of a department store it may be found that operating capital has been willing to pay 3 per cent, 3½ per cent, or even 4 per cent of the estimated net sales volume in dollars as rental for the real estate. Again, chain stores of the "variety" types will be paying, or are willing to pay, 5 per cent, 6 per cent, or even 7 per cent of net sales volume as rental.

It should be remembered, however, that the appraisal for reorganization purposes starts off basically with the knowledge that something is wrong. Maybe the entire trouble is financial; or maybe, and quite frequently, the difficulties are deep-seated and brought about, in part at least, by economic, social, or neighborhood shifts that at best can be but partially overcome under reorganizataion. Under such circumstances the usual "rule-of-thumb" standards are of doubtful help, and we are virtually forced to go into the business enterprise itself in order to value the assets properly.

RECONSTRUCTING THE BALANCE SHEET

In actual practice the public accountant will usually set up the reconstructed balance sheet as a test of business solvency as of any date. The appraiser's values may include the real estate and physical equipment only, or they may include many other assets such as inventories, investments in the securities of other companies, etc. The public accountant, however, assembles the figures from all sources and substitutes them for the book values where changes are indicated. Even the current items, such as accounts receivable, may be subject to adjustment in accordance with the probability of collection.

Upon the basis of such adjustments, but maintaining the company's status as to outstanding liabilities, including interest accruals and funded debt, the solvency or insolvency of the enterprise will be determined. It must be realized, therefore, what a tremendously vital part the appraiser plays in the game.

THE REORGANIZATION PLAN

And now we are back once more to the new deal for business afforded by the

former Amendment to the Bankruptcy Act, Section 77B, and now made more complete and workable under the Chandler Act. We are ready to reshuffle the cards and deal them out again to the various interests. The value of the "hole card" has been determined in our test for solvency and may now be turned up for all to see.

Setting aside from the discussion the many legal intermediary steps, it is at this point that the court begins its consideration of the various plans which may be advanced by the different interests, senior or junior bondholders, preferred stockholders, and finally common stockholders—equity capital. The "hand" that each interest is to receive will depend to a large extent upon the contribution the interest will make to the reorganized enterprise. The respective interests, of course, have proper rights to consideration in the order of their seniority, but even if the entire worth of the enterprise is found to be less than the face value of the first mortgage bonds, it does not necessarily mean that cards are refused to the junior interests or even to the stockholders.

If it appears that the retention of the former management (which had only an interest in common stock) is essential to or at least desirable for the fullest realization from the future operations of the enterprise, then a plan which permits the retention of some interest upon the part of the common stockholders may be approved. Naturally the desires of the various interests to get the best "hand" possible out of the "new deal" leads to long-drawn-out litigation. It is this phase, perhaps, that has been greatly improved under the Chandler Act. The Securities and Exchange Commission, now brought in as more or less of an adviser, *should* greatly strengthen and speed up the actual operation of the Act.

The Commission's influence, of course, remains an unknown factor up to the present writing. The Act is new. It provides that where the debt reaches $3,000,000 or more the plan must be filed with the Commission, this procedure being optional when the debt is less than that amount. One very significant question is whether the Commission is now equipped, or will become equipped, to consider properly the questions of valuation. We must admit that its practice to date in matters of public financing has not been encouraging. The Securities Act of 1933 will soon be six years old, and the Commission has not yet issued any concrete regulations relative to appraisals or even the basis of valuation on balance sheets submitted with financial programs. Accounting rules are quite comprehensive, but just so long as " book costs" are substantiated, the real value of the assets appears to have received little consideration.

Technically there should be no difference in principle between the base adopted for new financing and that for reorganization. The security holders still look to the property and its operations. The fair and reasonable value of the assets should be, in turn, the base upon which to construct proper financing. The fact that the Federal courts have become more familiar with the need for proper valuation in their administration of the former Section 77B may act as a strong incentive for the Commission to clarify its thinking in the matter, and then place its house in order as a more effective and constructive aid toward the administration of the Chandler Act.

A new deal for business! This is perhaps the most constructive piece of legislation that has ever been brought forth as an aid to financial and business rehabilitation. The appraiser has an increasingly significant part in the proper administration of the Act if the game is to be on the "up-and-up," as there seems every reason to believe it will be.

APPLICATION OF DEPRECIATION THEORY

VICTOR J. FREE, M.A.I.

A new thesis of depreciation was presented by Mr. Free in an article entitled "The Theory of Depreciation" in the January 1939 issue of the JOURNAL. He offers here a demonstration of this thesis.—Editors.

FOR the purpcse of demonstrating in appraisal practice the theory of depreciation presented in the January JOURNAL, two buildings have been selected—a four-family brick apartment and a single-family frame residence. The former lends itself to a further exposition of the belief that depreciation can be reasonably measured in money, instead of percentages of cost new. The latter affords an opportunity to present the usefulness of an economic check in the appraising of single-family homes.

This is not a demonstration appraisal. The reader is requested to assume that the properties have been appraised; that all useful data have been assembled, considered, and interpreted; and that attention is here directed to those data only which are directly concerned with depreciation and its measurement. Depreciation is considered to be loss of value from any cause and is presented in three types: physical deterioration, functional loss (obsolescence), and economic loss (obsolescence). It is assumed that the reader is familiar with these terms, the definitions of which are presented in *Appraisal Terminology*.[1]

Because buildings have finite lives, they are undergoing constant changes which affect their value. Deterioration of structure, change in art, or change through economic forces will assuredly influence conclusions concerning value. While depreciation manifests itself in three types, the appraiser may consider building life and value in two divisions—*accrued depreciation* and *remainder depreciation*. The former is that loss in value of a new structure which has occurred to the moment of appraisal; the latter is that loss yet to be sustained during remaining life. Remaining life may be physical (measured in time) or economic (measured in utility). Economic life is never greater, and may be much less, than physical life.

The appraiser seeks an estimate of the present worth of future benefits to be derived from ownership. He will make that estimate in money. If he can estimate accrued depreciation accurately and remainder depreciation with judgment, he will reach a conclusion that is reasonable. The sum of these divisions of depreciation equals building value over its entire life. (The writer is not forgetful that at the end of estimated physical or economic life there may remain some residual building value through salvage in demolition or in reconstruction. Its measurement in the value estimate will depend upon varying conditions that must be considered in the immediate problem in appraisement.)

FOUR-FAMILY APARTMENT

Physical description: The four-family apartment property is located five miles from the business district of a middle western industrial city of 1,000,000 people. It is a brick-veneered building, thirty-six by sixty-two feet on the foundation and thirty feet in height. There is a four-car brick garage with a full cement drive. The landscaping is limited. The building has a center entrance with hallways extending to the rear of each floor, dividing the space into four suites, each containing

[1]Education and Research Committee, American Institute of Real Estate Appraisers, *Appraisal Terminology* (2nd ed., Chicago, 1938).

living room, dining room, large kitchen, two bedrooms, and bathroom. There is an outside rear stairway of iron frame and steps, leading from the second floor to a paved rear court. A rear service entrance leads to the basement, and a small rear porch of wood is provided for each suite. The roof is flat composition. All sheet-metal work is galvanized iron. There is a small amount of stone ornamentation at the doors and windows. The basement is under the entire building and has a seven-foot ceiling clearance; the floor is of cement and the ceiling plastered. Construction is in conformity with good practice. There are separate hot-air heating units, fueled with coal—a well-planned installation with adequate outlets. Each suite has a gas-fired heater for hot water. There are laundry facilities and lockers. All water lines are galvanized iron. Electric installation is of the knob and tube type.

In the suites, the floors are oak over diagonally laid, pine subflooring. Walls and ceilings are papered over plaster. There is oak trim in the living and dining rooms and pine trim elsewhere. The bathrooms have oak floors; the lower walls are Keene cement, the remainder, paper over plaster. The tubs are on a base, but not built in. There are wall-attached wash-bowls and ordinary toilets. Electric fixtures are old and base receptacles inadequate.

The garage is thirty-six feet by eighteen feet. It has a cement floor, and a flat, paper roof.

The property belongs to an absentee owner and has been neglected. It was built in 1924.

Neighborhood: This neighborhood, which was solidly built fifteen years ago during rapid industrial expansion, has good transportation, good schools and churches, and fair neighborhood stores. Earning levels and rent-paying ability have fallen rapidly for several years. Considered very desirable, when new, for professional and business people, it is now populated by mixed foreign and native-white families of lower social status and earning power. When new, these suites were rented for $70 each per month. In 1928 they brought $75 a month and are now rented for $45 a month. The only vacancy for three years has been the loss of three months' rental of one suite.

Reproduction cost:

Present cost of building new			$18,750.00
Present cost of garage new			700.00
Present cost of landscaping			200.00
Value of land (demand price)			3,000.00
Total reproduction cost new			$22,650.00
Depreciation:			
Physical deterioration	Curable	$2,500.00	
	Incurable	1,200.00	
Functional loss	Curable	2,200.00	
	Incurable	1,500.00	
Economic loss		4,800.00	12,200.00
Indicated present value			$10,450.00

Physical deterioration is computed: (a) in cost to restore this building in so far as may be necessary to preserve tenancy, correct deferred maintenance, and arrest a more rapid loss in the future and (b) in estimation of loss through gradual wearing out of materials. (This is the only estimate of an intangible nature appearing in the procedure.) The cost to cure observable depreciation is reached by a complete quantity analysis of labor and materials. Loss through disintegration is very small in amount. Buildings well maintained *tend* to continue in perpetuity. The amount estimated is principally for loss (incurable) in equipment, which must sometime be renewed.

Curable functional loss is represented in outmoded bathrooms and kitchens. The estimates include completely reconditioned bathrooms and modern breakfast nooks as part of the present large kitchens. The law of profitable contribution is satisfied

in this expenditure. *Incurable functional loss* is estimated in terms of sales or rental resistance. In this property it consists of poor room layout and a narrow stairway to the second floor. It is estimated here for purposes of the reproduction cost approach. In the economic approach it is accounted for in the net income under the building residual procedure.

Economic loss is computed by capitalizing the rental loss sustained by this building by reason of a changing type of population. Failure to produce normal income, by comparison with a similar building in a neighborhood which has not been depleted, is the indication of economic loss. If this building were upon land of equal value two miles easterly, rentals of $55 per month per suite could be secured readily. This loss, amounting to $480 per year in the building, is capitalized at 10 per cent, determining an economic depreciation of $4,800. (The high rate of 10 per cent is used because, with higher rentals, greater operating costs and increased taxes may be expected.)

Measured in money: Attention is directed in this analysis of accrued depreciation to these things:

1. No age — percentage computations are used.
2. No unreasonable hypothesis is set forth, and no vague assumption is made.
3. Unsupported estimates are not used, and economic inutility is not made a factor (percentage) of cost new. It is presented as a loss of value in money through economic change.
4. Accrued depreciation of all types is determined by observation, and each type estimated in money.
5. Over-all percentage of depreciation (if the appraiser must have it) is 60 per cent or 4 per cent per year upon this building.

Remainder depreciation: In the foregoing analysis evidence of accrued depreciation is presented and such depreciation measured in money by observation. This is necessary in order to estimate by the reproduction cost approach the present value of the property. No appraisal by this approach can be made better than its comprehension, analysis, and treatment of accrued depreciation. This building now has remaining for utility 40 per cent of its cost to create new. That is interesting information — not wholly conclusive in so far as market value is concerned. Depreciation has been studied and estimated for that period of building life which has elapsed. More important is that period which remains. What value in terms of money does it now have?

Whatever of value the building may now have is measured by its remainder depreciation. If provision is made in the treatment of income for the return of capital in the building, such capital will be fully returned when economic life ends, and such return will be the sum of estimated annual losses through depreciation during remaining life. Three concepts have been evolved for measurement of this remainder depreciation—all procedures in the economic approach to value:

1. *Straight-line depreciation process,* in which the depreciation rate is added to the interest rate in the capitalization of net income, returning equal amounts of capital (depreciation) annually.
2. *Sinking-fund process,* in which an annual sum is set aside to accumulate at compound interest, thus restoring capital (depreciation) at the end of the economic life.
3. *The annuity process,* in which a portion of capital (remainder depreciation) is returned each year—a small sum in the early part of economic life and increasing in

amount as interest becomes less.

Level of net income: This writer has little confidence in conversion factors except when applied to *net income*.

"How many times the gross income?" asks an anxious valuator.

"Three to eleven," is a fair answer.

Where, between these figures, the correct multiple lies may not be known to angels or men until all the evidence is accumulated. Net annual income before depreciation may be determined by deducting from gross income all charges properly imputable to operating costs, fixed charges, and a reserve for replacements. When that is done, the appraiser has one tangible bit of evidence—a place from which to start, a beginning that has promise of a reasonable conclusion.

The reader is requested to believe that careful study has resulted in proper deductions in so far as this problem in appraisal is concerned. Gross income is $2,160 per year; gross effective income is $1,944 per year; net income before depreciation is $980 per year. Ratio of net income to gross effective income is approximately 50 per cent. Buildings of this type in midlife, where suites are individually heated at tenant expense, *tend* to show such a relationship in the city and under the conditions here existing.

Economic life: When the appraiser estimates remaining economic life, he is fixing the time within which building value (remainder depreciation) is to be returned, whether his process is straight-line, sinking-fund, or annuity. Therefore, remaining life is one estimate which the appraiser must make. Upon its relative accuracy the appraisal must depend for reasonableness.

The neighborhood of this apartment is stabilized. The character of population should not materially change for thirty years. Earnings and ability to pay rent will not vary greatly. Boom periods in industry will bring increases; depressions will level them out. That has been history over the past thirty years. There is little to indicate that history will be changed. The building is structurally sound. With good maintenance, as herein provided, it should continue to be a satisfactory utility for the economic life indicated.

Capitalization rate: After estimation of economic life, the selection of a capitalization rate is necessary, whatever treatment of net income may later be determined. None of the five major processes indicated in the prior article, "The Theory of Depreciation," is more important. It is understood that at this point in the procedure the net income before depreciation has been calculated and the remaining economic life estimated. Whether the "band of investment" theory is invoked or whether the combination of "safe rate, rate for risk, and rate for service" or any other thesis is adopted, there remain comparisons with interest paid on similar securities, prevailing rates of income from similar properties sold, and trends of commodity markets, bonds, and real estate mortgages. Risk to capital is always predominant and not to be forgotten. In the property under discussion, capitalization rates of 6 per cent for demand land price and 7 per cent for the building have been selected.

Conversion factors: Determining the manner in which capital (remainder depreciation) shall be returned to the investor involves selection of factors in conversion from one of three widely known tables, in which the present worth of one per annum at a given interest rate is computed for any number of years. These tables are based upon *The Compound Interest Valuation Premise* by Inwood, *The Sinking Fund Valuation Premise* by Hoskold, and *The Declining Annuity Tables of Factors* by Babcock. They have major significance and differences as follows:

Inwood: Contemplates level annual return over building life; interest and part payment of principal (remainder depreciation) are returned each year.

Hoskold: Contemplates level annual return over building life; each part payment of principal is set aside in a sinking fund to accumulate at compound interest annually, restoring capital in one sum at the end of building life.

Babcock: Contemplates that most annuities decline in conformity with a curve, reaching zero at the end of economic life. Capital return (depreciation) is in part each year. Each of these premises provides in its factors both for interest at a selected rate and for the return of invested capital during economic life.

In a consideration of the appraisal here presented, a factor from *The Compound Interest Valuation Premise* of Inwood has been selected. Argument in its favor includes the belief that over a period of thirty years total net income will amount to the present worth of the annuity selected. It is not expected that annual net realization will be at the same fixed figure each year for thirty years. It is reasonable to believe that boom, depression, and normalcy may all appear in that period. But it is believed that an average annual income will be secured, which, in the life of the building, will return interest and remainder depreciation, thus restoring capital.

The fifth and last major operation in the economic approach is the selection of a procedure in the conversion of an annuity into an opinion of value. There are three such procedures, known as *land earnings residual, building earnings residual,* and *property earnings residual with land reversion.*

Land earnings residual: Used when a building is new and is the highest and best use of the land, or when land value is to be determined by a hypothetical best use building.

Building earnings residual: Used when a building is older and there is evidence of over-, under-, or misplaced improvement; when obsolescence is evident, functional, or economic.

Property earnings residual (land reversion): Used when the end of economic life is near; when reversionary land value may be accurately estimated.

The selection of a procedure is readily made in the present appraisal. The building is suffering from losses, economic and functional. It is the major part of value. Land value is known; building value is the unknown quantity. The building earnings procedure lends itself well to this problem.

A summary of major operations for this appraisal follows:

1. *Net annual income* before depreciation, $980.
2. *Remaining economic life,* thirty years.
3. *Capitalization rate,* 6 per cent for land, 7 per cent for building.
4. *Conversion factor,* Inwood's *Compound Interest Valuation Premise.*
5. *Procedure,* building earnings residual.

From this point forward it is a simple mathematical problem with results as follows:

Imputable to land (6% of $3,000)	$ 180.00
Imputable to building	800.00
	$ 980.00
$800 x 12.409 (Inwood factor)	$ 9,927.00
Land (by comparison)	3,000.00
Total	$12,927.00
Less deduction for curable deterioration	2,500.00
Total	$10,427.00

Sold for $10,500: The property was worth $10,500, was appraised for $10,500, and was sold "within a reasonable time" for that amount. Attention is directed to the fact that no "reconciliation" estimates were necessary. A check of depreciation by observation indicated accrued depreciation at the time of appraisal, and the reproduction cost approach foreshadowed

an estimate of value. The economic approach followed and suggested the same value estimate. It *is* possible to estimate accrued depreciation in money—not percentages; it *is* possible to estimate present worth of future (money) benefits by the technique of the capitalization approach to value. In no serious degree is variation necessary. In a hundred appraisals of income property no "adjustments" have been found to be indicated; no lump sum has been "lopped" off to make dissimilar results appear similar. "Upon these things have I relied; in them have I placed my trust."

SINGLE-FAMILY FRAME RESIDENCE

It is generally believed and frequently stated that the economic approach to value has no place in the appraisal of single-family homes. Considered only in comparison with valuation procedure in a property dependent upon income for its value, there is much to support the statement. However, the purchase, ownership, and occupancy of a home is a venture into the field of economics for those who undertake it. Does such a venture have a reasonable foundation in sound economy, or must the appraiser depend wholly upon desire, amenities, and reproduction cost less accrued depreciation? It is true that government agencies and some mortgage lenders rely upon a multiple of gross monthly rental, actual or potential, to confirm findings of the reproduction cost approach. It often happens that such multiples (100 or 120) produce results consonant with reasonableness. But reliance may no more be placed therein than in a multiple of gross income from an apartment building.

It appears possible that appraisers, denying virtue in the income capitalization approach for the single-residence appraisal, have overlooked something important in the capitalization rate. The owner or prospective owner of a home may not expect, nor be entitled to receive, an interest rate indicated for risk investment or speculation. Equity position in investment or speculative fields commands a high return. Equity position of a home purchaser connotes a low interest return, comparable with what might be expected from government bonds, savings accounts, or life insurance. This is more clearly indicated by a modification of the "band of investment" method of determining fair capitalization rates in the following manner:

INCOME PROPERTY			
First mortgage	60% @ 5%	=	3.0%
Second mortgage	20% @ 8%	=	1.6%
Equity	20% @ 12%	=	2.4%
INDICATED RATE			7.0%

SINGLE-FAMILY RESIDENCE			
First mortgage	70% @ 5%	=	3.5%
Second mortgage			None
Equity	30% @ 3%	=	0.9%
INDICATED RATE			4.4%

Considerations of risk: It is reasonable to believe that the differing rates thus indicated are justified in valuation procedure. The purchaser of an income-producing property is adventuring with risk. His capital is earmarked for profit. When risk is apparent, capitalization rates rise. Conversely, when risk is negligible, capitalization rates fall. When an appraiser estimates economic valuation by considering one hundred times the monthly income, he means that his gross capitalization rate upon an annual basis in 12 per cent. It tends to be reasonable, although there is no sound appraisal practice when an "average" figure is invoked in application to every property. Attention is directed to the following single-family residence.

Reproduction cost approach: The property is located in a middle western city of industrial character and is twenty-five years old. The house has lap siding exterior, slate roof, and stone foundation. Gutters and downspouts are galvanized iron. It is twenty-six by thirty feet on the

main foundation and thirty feet in height, containing 23,400 cubic feet. The first floor has a living room, dining room, and kitchen; the second floor, four bedrooms and an old-type bathroom. The full basement has cement floor, is equipped with adequate lighting, and contains a hot-air heating unit, coal fired. There is a sixty-gallon hot-water tank, serviced by an ordinary gas burner. All water lines are galvanized iron. Electric wiring is of the knob and tube type. Outlets are inadequate, and fixtures are outmoded. The floors are single three-quarter-inch oak; the trim downstairs is oak and that upstairs is pine. Doors and windows are second-grade. No outside openings are weatherstripped. The third floor is an unfinished attic. The bathroom has lower walls of Keene cement, with paper over plaster above. The bathtub is on legs, the washbowl is wall-attached, and the fixtures are No. 2 Standard Sanitary grade.

There is a one-car garage, with a slag and cinder drive. The landscaping is of no permanent value.

Neighborhood: This was a good middle-class neighborhood when the subject property was built twenty-five years ago. The panorama of change in an industrial city has brought people of lower social standing and earning power. The neighborhood is four miles from the center of the city; it has good transportation facilities and convenient schools, churches, and stores. A population inventory shows that 52 per cent of the people are Jewish, 4 per cent are Negro, and the other 44 per cent are of mixed nationalities, both foreign- and native-born.

This is a condensed word picture of what the appraiser sees every day in cities of the same character. What is its value?

Reproduction cost data:

Cost new today 23,400 cu. ft @ 32c		$7,488.00
Cost of garage and driveway		250.00
Cost of land (demand price)		800.00
Total reproduction cost new		$8,538.00

Depreciation (house and garage):

Observed physical deterioration (curable)	$2,500.00	
Incurable physical deterioration	1,000.00	
Functional loss (curable)	300.00	
Economic loss[2]	900.00	
		4,700.00
Indicated present value		$3,838.00
Say—		$3,850.00

Economic approach: This property at the time of examination was occupied by a tenant who paid $40 per month rental. Examination of this rental in the interest of a proposed purchaser resulted as follows:

Annual gross income			$480.00
Operating costs annually:			
Maintenance	$100.00		
Water	16.00		
		$116.00	
Fixed charges:			
Taxes	$62.00		
Insurance	14.00		
		76.00	
Total charges (per year)[3]			192.00
Net income before depreciation			$288.00
Imputable to land 4.4% of $800			35.20
Imputable to building			$252.80

Assuming straight-line depreciation of 4% per year (building life of 25 years) and using a capitalization rate of 4.4%:

[2]The difference between the rental assigned in the economic approach and the cost of occupancy to the owner in the economic check occurs because of differing methods of treating remainder depreciation. In the first instance, where building value was unknown, the capitalization rate discovered it. In the second procedure, with the probable building value indicated, the return of capital was provided by a sinking-fund method.

[3]The owner will manage his own property. There will be no vacancy. Ordinary maintenance charges are less. In these respects an operating statement for single-family residential property, owner-occupied, differs materially from such a statement for speculative income.

Building value	$3,010.00
Land value	800.00
Total indicated value	$3,810.00

The purchaser was advised to pay $3,750 for the property. He bought it and financed it as indicated in this procedure, and at this moment everyone is happy!

This process, reversed to indicate the cost to a purchaser in terms of monthly rental and providing for the return of his building capital during the economic life of the building, becomes a sound sales argument for the Realtor-appraiser. It may be presented as follows:

Interest on investment of $3,750 at 4.4% per annum	$165.00
Operating costs and fixed charges per annum	192.00
Annual sum in sinking fund at 3% compound interest to return building value in 25 years	81.00
Total annual cost to owner-occupant	$438.00
Cost per month in terms of rental	$ 36.50

A USEFUL CHECK

The reader will observe that there is little discrepancy in this procedure between the reproduction cost approach and the economic check in so far as indication of value is concerned. It is respectfully submitted that *there should be little difference.* If either of these approaches has value to the appraiser, if either of them carries conviction to the client, it must be reasonable and within the zone of a reasonable value estimate. Adequate data, studied interpretation of data, observed accrued depreciation, measurement of loss in money brought a reproduction cost estimate. A carefully estimated net annual return, the selection of a reasonable economic life, the discovery of a fair capitalization rate, and present building value (remainder depreciation) emerged as tangible evidence of value.

It is not assumed that the valuation process is solved by these presentations of theory and practice in determining depreciation, accrued and remainder. The writer has applied these principles in estimating value in many properties over a period of three years. Uniformly, there have been results more nearly satisfactory than were ever found in age-percentage procedures. This is especially true where obsolescence has appeared and where neglect of property is manifested. If the procedure is worthy of recognition, it is because pure guesswork is largely eliminated. Those phases of depreciation where estimate only is possible have been reduced in number and significance. Reliance is placed in that which is observed, that which is reasonable, and that which is of good judgment.

THE SMALL-TOWN HOTEL

EUGENE H. FRIES

IT was late afternoon on a hot summer day of 1926 in the city of Rolling Prairie, Iowa. Tom Jones, the town's leading men's clothier, had closed his store adjacent to the old Central House. As was Tom's custom, he walked to the corner where the rocking chairs were creaking on the sidewalk. He was part owner of the hotel. His grandfather had contributed a portion of the land and capital when the Victorian facade of the Central House began to rise, long before the turn of the century. The hotel, once the pride of Rolling Prairie, was now a weather-beaten, old brick building with high ceilinged rooms, creaking stairs, and protesting floors. Of the forty rooms, only six (those on the corners) were equipped with bathrooms—the guests in the others customarily "stood in line."

Tom spotted a vacant chair and carefully settled his weight on the wooden seat. The usual discussions were under way. This time the question of a new hotel was paramount. Perhaps it was the heat—at any rate, Tom, contrary to his usual habit, allowed himself to be drawn into the argument and, somewhat against his will, *almost* agreed that a new hotel was a civic duty.

The next morning Tom arose, a citizen *convinced*. He visited Jim Brady at the First National Bank. There were interviews with the town's other leading citizens. Enthusiasm grew. The local civic bodies got behind it. Arrangements were made with a Davenport bank to take the bond issue. The local community subscribed to the common stock. Tom Jones took stock for his equities in the Central House and his adjoining store property.

In the spring of 1927 the ground was broken for the new 100-room hotel. Plans for the "Cornstate" were drawn by a Chicago architect specializing in hotel construction. Contrary to his best judgment, the majority of the rooms were planned with private bathrooms. The civic clubs, remembering the inadequate dining and assembly rooms of the old hotel, were responsible for the large coffee shop on the first floor and the banquet and dining rooms on the mezzanine floor. These and other recommendations were carried over the architect's objections.

Just before the concrete footings were poured, the engineers were asked to redesign the structure to provide carrying capacity for three additional floors—the new hotel would then be prepared should the space be required at a later time.

THE "CORNSTATE" OPENED FOR BUSINESS

The grand opening of the "Cornstate" coincided with the celebration of the harvest festival. A carnival and street parade provided an outlet for the more energetic of the populace. The city's elite gathered under the crystal chandeliers of the new ballroom for the evening's festivities. Tours were conducted for the eager visitors. In the basement they viewed the boiler room, spic and span with heating boilers, pumps, and other equipment; the public toilets glistening with tile floors, marble walls, and china plumbing fixtures; the storage rooms bulging with hotel and restaurant supplies; and the new six-chair barbershop.

The first floor displayed its high-ceilinged lobby in the Renaissance style, with the huge fireplace and frescoed ceiling decorations; also the hotel offices, the modern coffee shop, and six retail stores.

The mezzanine floor was devoted to a large ballroom with serving kitchen, check room, writing room, and private dining room.

Above the mezzanine floor the building receded from its rectangular shape and assumed an "L" form, following the frontage on Main and Central Streets.

The upper floors from the second to the fifth proved to be a model of uniformity. There were twenty-five rooms per floor, each with outside exposure—twenty with bathrooms and the others with toilet and lavatory.

The townsfolk exclaimed in pleasure at the deep-piled carpeting and the harmonious and comfortable furnishings. Descending in the swift-moving electric elevator they voted the hotel a success and a credit to a city of 15,000 population.

THE OUTLOOK

The years 1928 and 1929 proved to be good for business. Hotel operations were profitable. The interest and amortization on bonds, minor debts, and common stock dividends were paid.

Tom Jones was now the president of the hotel company; he also conducted a prosperous clothing business in the new streamlined store adjacent to the lobby.

During the late fall of 1929 the crash of the security markets, reverberating throughout the nation, caused echoing forebodings in the fertile prairie country. Business dropped off during the spring of 1930, although everyone was still optimistic. As time rolled on, however, the shadows of the depression steadily deepened, and gradually the hotel operations grew less and less profitable.

Tom Jones's business also dropped off to the vanishing point, so he took over the management of the hotel and replaced some of the professional hotel employees with local help. Matters went from bad to worse. Interest on the bonds went into default; dividends were passed; taxes remained unpaid; painting and decorating were deferred; linens and furnishings were replaced only as a last extremity; and a general state of neglect gradually settled over the hotel enterprise. The dark days of 1933-34 came and passed, bringing bank closings and moratoriums. Eventually business improvement set in. However, such improvement as came to the hotel failed to bring the enterprise out of the "red." The bondholders finally lost patience, and a period of litigation began.

Tom Jones retained the management of the hotel until such time as a sale might be consummated and confirmed by the courts. It was his hope that a plan might be worked out by which it would be possible to reorganize and save a portion of the equity of the stockholders.

Up to this time the original cost had been thought to represent the value of the hotel, lessened, of course, by such depreciation reserves as had been set up on the books. These reserves had been entered upon the basis of normal annual rates during the good years and lesser amounts, if any, during the later and leaner years. Everyone now agreed that the depreciated book costs no longer expressed the true measure of the value of the property. It was evident that they were not supported by earnings. It was also known that prices of materials and labor had descended and income had dropped, but that certain operating costs had steadily increased—which presented a confusing picture indeed.

EXPERIENCED APPRAISERS EVALUATE "CORNSTATE"

In order to clarify the situation, valuations were made by several of the local

people, none of whom had had any experience with this type of property. As a result, the estimates were in disagreement and confusion reigned as to the basic valuation principles involved. In order to ward off confirmation of the sale and permit reorganization, the court required presentation of evidence of a fair market value. At this point a decision was reached to call in independent professional appraisers familiar with the valuation of hotel properties, and several days later the morning westbound sleeper deposited two appraisers on the station platform in Rolling Prairie. Within a few hours they had contacted Tom Jones and obtained from him the necessary plans and specifications of the hotel buildings, access to all books and statements of account, and permission to inspect any and all parts of the hotel for the purpose of making the valuation of the property.

The appraisers explained that one of them was a specialist in the valuation of furniture and furnishings, the other, in land, buildings, and economics; and that it was customary for them to work in close co-operation with each other to ascertain the facts upon which a provable valuation could be founded. They also advised Tom Jones that in valuing a hotel enterprise there are really two separate and distinct enterprises to consider: (1) the hotel operating enterprise, assumed to be the owner of hotel furniture and furnishings necessary to carry on a hotel business in a building for which the enterprise is expected to earn an income if owned—or a rental if leased; (2) the building or real estate enterprise, to which is allotted the rental from hotel operations, retail stores, or other agencies which are renting space in the building.

Each of these enterprises is considered on its own merits. However, the hotel enterprise is conceded to have prior rights to assignment of income because the continued use and value of the hotel building depend principally upon the success of the hotel operations for its primary revenue in the form of residual income or rental. When the residual or rental income available for the building is sufficient to support the physical or maximum value of the building and fixed equipment based upon replacement cost less depreciation, then the latter becomes synonymous with the *fair market value*. When the residual earnings are in excess of the amount required to support the physical building value, the excess earnings have a tendency to increase the value of the hotel enterprise and not the building value. They may be attributable to intangible assets built up through efficient management. When the residual earnings or rentals are insufficient to provide a fair return on the physical value, the latter is lessened by the capitalized amount of the earning deficiency.

Desirability of location, design and arrangement, and the state of repair of the hotel property are major contributory factors in the endeavor of efficient management to produce sufficient revenues which, after payment of hotel operating costs and management fees, will leave a residue applicable to the real estate in the form of rent. Deferred repairs and maintenance are subject to correction. However, disadvantageous location, poor design and arrangement, as well as excess construction, are generally a permanent liability not subject to relief.

Again, a desirable hotel property, not burdened with locational or physical disadvantages, may be encumbered by an inefficient hotel operation. Because of its priority of claim, this operation may dissipate the earnings rightfully assignable to the hotel building in the form of rent.

This type of encumbrance is subject to correction by replacement with efficient management; and the unfavorable earning statements may be adjusted for valuation purposes to reflect the potential savings possible under a change of management.

It is thus apparent that, whenever the hotel and building operations are conducted as one business under the same management, it becomes a prime necessity to analyze the operations of each as a separate enterprise.

The Cornstate Hotel was being operated in this manner. Tom Jones could now readily understand why the appraisers found it necessary to go to the books of account for data on revenues and expenses. His hotel enterprise was not paying a stipulated rental for the hotel premises, and he had no conception as to what a fair rental might be.

THE VALUATION PROCEDURE

The appraisers adopted the following procedure in the execution of their work:

1. An investigation of the current fair market value of the land.
2. An estimate of the cost of replacement new and cost less depreciation of the building and building fixtures.
3. An appraisal of the hotel furniture and furnishings upon the basis of their sound value for continued use as a part of an operating hotel enterprise.
4. An analysis of hotel revenues, expenses, and other charges to determine the residue applicable to the building as rental.
5. An estimate of the value of the building based upon its capital value as supported by income applicable thereto.
6. A summation of the current fair market value of the land and building and the fair value to a going concern of the hotel furniture and furnishings, which in total should represent the fair market value of the entire hotel enterprise.

The records disclosed certain interesting data, as follows:

Cost of fixed assets as of 1927:	
Land	$ 50,000.00
Building	275,000.00
Furnishings	48,500.00
Total	$373,500.00
Capital structure:	
First mortgage bonds	$210,000.00
Common stock	190,000.00
Total	$400,000.00

The appraisers prepared a physical valuation in considerable detail, which was summarized as follows:

APPRAISED INVESTMENT AS OF DECEMBER 31, 1938

	Cost of Replacement	Cost of Replacement Less Depreciation
Land	$ 30,000.00	$ 30,000.00
Building and fixed equipment	230,000.00	160,000.00*
Furnishings	44,000.00	25,000.00
Totals	$304,000.00	$215,000.00

*Subject to adjustment upon fair market value basis unless supported by earnings.

The percentage of occupancy varied from a high of 55 per cent to a low of 25 per cent for the period from 1930 to 1938, inclusive.

The system of accounting set up by a local accountant proved to be greatly at variance with modern hotel accounting practice. The operating expenses were itemized for certain groups and lumped together for others. The latter items were in important amounts and appeared under the heading of miscellaneous expense. It proved impossible to gain a clear conception of expense by normal hotel depart-

ments from the available records. The appraisers found it necessary, therefore, to reconstruct the profit and loss statement. This was intended to reflect:

1. The income potentialities as demonstrated by the hotel over a representative period of years, but tempered by reasonable future expectancies reflecting the economic outlook for this particular hotel and community.
2. The hotel operating costs, using:
   A. Actual costs where such costs could not reasonably be expected to be lessened by any other type of management.
   B. Estimated costs for all other expenses, commensurate with normal hotel costs incurred under efficient management operating a hotel of this price class and under a 50 per cent average occupancy, the maximum average expectancy in this case.

The analysis of the property and the accounts clearly demonstrated:

1. That the hotel had a decided overcapacity resulting in excess heating, lighting, maintenance, and decorating costs, as well as excess taxes and insurance.
2. That it was inefficiently managed as evidenced by the fact that operating expenses were in excess of average expenses for other hotels of the same income class per room and operating at the same percentage of occupancy.
3. That the repair and maintenance policy was substandard and that steadily increasing repair and maintenance costs could be reasonably expected.

The appraisers' estimates of future operations, as predicated upon the investigation and analysis, were set up as follows:

RECONSTRUCTED PROFIT AND LOSS STATEMENT

(BASED UPON ADJUSTED INCOME AND EXPENSE EXPECTANCIES)

Income from rooms (five-year average)		$35,500.00	
Room expenses*		14,000.00	
Room department profit			$21,500.00
Income from restaurant		$30,200.00	
Cost of goods sold	$18,500.00		
Restaurant expenses	12,000.00		
		30,500.00	
Restaurant profit			None
Income from tavern		$20,300.00	
Cost of goods sold	$10,200.00		
Tavern expenses	6,800.00		
		17,000.00	
Tavern profit			$ 3,300.00
Miscellaneous income (five-year average)			1,200.00
Total gross profit			$26,000.00
General expenses*		$ 2,500.00	
Heat, light, and power*		6,200.00	
Repairs*		2,800.00	
Total deductions			$11,500.00
Gross house profit, exclusive of income from stores and before taxes and depreciation			$14,500.00

*Computed from details based upon normal hotel operating costs.

This analysis indicated a gross house profit of $14,500 from the operation of the hotel. The restaurant department, true to average hotel history, was not profitable, but was considered an essential adjunct contributing indirectly to the income from room sales.

In addition to the total direct cost of operating the hotel, provision was made for:

1. Return on the fair value of the investment in furnishings.
2. Depreciation charges to amortize the cost of furnishings over their useful lives.
3. Return on working capital commensurate with the risk of the investment.
4. Compensation to management.

RESIDUAL FAIR RENTAL FOR HOTEL PREMISES
(EXCLUSIVE OF STORE RENTALS)

House profit		$14,500.00
Return on fair value of furnishings ($25,000 @ 10%)	$2,500.00	
Depreciation on furnishings ($44,000 @ 7½%)	3,300.00	
Return on working capital ($3,000 @ 10%)	300.00	
Total deductions		6,100.00
Net house profit		$ 8,400.00
Compensation to management		3,600.00
Remaining for rental of real estate per annum		$ 4,800.00

The fair market value of the building was determined, based upon the following:

Hotel rental	$4,800.00	
Store rentals	6,500.00	
Total income for real estate		$11,300.00
Less real estate taxes		3,300.00
Return to real estate		$ 8,000.00
Less return on land (5% on $30,000)		1,500.00
Return to building (Insurance and repairs by hotel)		$ 6,500.00

Capitalization: Under normal economic conditions the hotel appeared to have a reasonable life expectancy of perhaps thirty to thirty-five years. After a full consideration of all of the circumstances, the hazards in the several estimates, and the returns then being anticipated from investments of equivalent risk, the appraisers adopted 8 per cent as an over-all rate applicable to the building, which was to provide a fair return plus depreciation or amortization of the investment over its reasonable economic life expectancy:

$$\frac{\$6{,}500}{.08} \text{ equals } \$81{,}250.00\ *$$

*Appraisal investment as of December 31, 1938; $160,000 reduced to fair market value of $81,250 because of insufficient earnings.

SUMMATION OF FAIR MARKET VALUE OF HOTEL ENTERPRISE

Land	$30,000.00	
Building and fixed equipment	81,250.00	
Furnishings	25,000.00	
Total fair market value		$136,250.00

THE RESULTS

The appraisal figure was far from gratifying to Tom Jones. The original investment in fixed assets in the amount of $373,500 had shrunk to an appraised investment of $215,000 at December 31, 1938, owing to lower price levels and accrued depreciation. This had been further reduced because of inadequacy of income, either demonstrated or potential, to a fair market value of $136,250.

Tom was finally convinced that the entire equity of the stockholders had been wiped out and that the bondholders would probably suffer a considerable loss through liquidation of the holding.

Realizing the futility of further court proceedings, he made his peace with the bondholders and prepared to re-enter the clothing business in the city of Rolling Prairie. To gallant Tom Jones we wish better luck in his new endeavors.

CAPITALIZATION

ROBERT H. ARMSTRONG, M.A.I.

THE valuation of real estate by means of the income capitalization method has come into wide vogue during the past ten years. This method of valuing income-producing properties, when embellished, embroidered, and finally polished to a high luster, seems flawless in its argument and faultless as to its reasonability. To those not educated or admitted into the higher realms of valuation procedure mysticism, capitalization seems not to supply *an* answer—it supplies *the* answer!

Now it is not the purpose of this article to deprecate this widely used method of appraising which depends exclusively upon income. Income *may* be an element through which value may be determined—in fact, income may even be the element by which value *is* determined—but capitalization *per se* does not and cannot determine value in a capitalistic economy. Income might determine value in a static state, but it cannot be the sole criterion of value in any economic system that the world has so far known. Therefore, it is the purpose of this article to explore some of the weaknesses and defects of the capital value theory, for perhaps by understanding these faults better, we can use capitalization more accurately and more successfully as a gauge of value.

In all transactions for goods and services, buyers and sellers use rough methods of capitalization. The process is carried on in a manner which is empirical rather than by quantitative and qualitative measurements.

In the field of real estate appraisal, however, attempts are being made to refine the capitalization process to a point whereby the present worth of future benefits can be accurately estimated. In the last analysis, then, professional reputation will rest on the degree of accuracy with which forecasts are made.

There have been a number of definitions of capitalization. Dr. Frank A. Fetter defines it as "the process of calculating the market price of salable incomes."[1] Prof. Irving Fisher, the other leading exponent of the capital value theory, states that it is "the process of discounting by which expected income is translated into present capital-value. Usually employed only when the income is considered uniform and perpetual, in which case capitalization consists in dividing the rate of income per annum by the rate of interest."[2] Dr. Fetter and Prof. Fisher were two of the first economists in this country to expound the doctrine of capitalization. Economists in general have neglected this problem.

It should be noted that Prof. Fisher uses the words, "employed only when the income is considered uniform and perpetual." In the case of high-grade bonds or well-secured leaseholds, it will be granted that income may be uniform and perpetual, but this most assuredly is not the case in the majority of properties which appraisers are called upon to value. The *theory* of capital value depends upon value as representing the present worth of future benefits, but if the future benefits are not uniform or perpetual, then how can they be capitalized? It is true that rough estimates of a presumed, stabilized income may be made and that this type of income may be capitalized (again presuming the correct rate of interest is chosen), but the question may well be asked: "How competent is the average appraiser to assess the future, particularly in the light of economic fluctu-

[1] Frank A. Fetter, *Economic Principles* (New York: The Century Co., 1922), p. 267.
[2] Irving Fisher, *The Nature of Capital and Income* (New York: MacMillan Co., 1906), p. 330.

ations?" Of course, past history can be of aid, but there is little doubt that the measurement of the future cannot be solved by *a priori* methods.

When capitalization is used, another element which must be measured is that of risk. How absurd it is to believe that we may continually invest at a safe rate, even as low as 4 per cent, may be gleaned through the following example: If $1.00 were invested at a 4 per cent compound interest rate in the year 1000, it would amount to $2,500 in 200 years; six million dollars in 400 years; fifteen billion dollars in 600 years; forty trillion dollars in 800 years; and in a thousand years, this one-dollar investment would amount to one hundred quadrillion dollars. In other words, even in a nation as prosperous and as progressive as is the United States, wealth accrues at a rate millions of times slower than does 4 per cent interest. Therefore, capitalization must deal with the near and immediate future, for it is extremely unlikely that we can reasonably expect our very modes of life to remain unchanged for periods even so long as a single decade.

BUSINESS CYCLES

The use of capitalization seems to be most definitely proscribed by the business cycle. However, before examining the relationship between capitalization and the business cycle, it is necessary to have an understanding at least of some of the simpler movements of the cycle.

It is a well-known fact that business is never static. Production, consumption, prices, and the values of all commodities are eternally changing, and the business cycle is sometimes defined as the periodic expansions and contradictions of business, in which there are involved characteristic phases of maladjustment and readjustment. As the changes in business occur, there is usually the pervasiveness of wave motion, with the waves varying both in length and in amplitude. Generally speaking, the cyclical oscillations are fairly regular in their phases, and the phases of the cycle in their sequential order are prosperity, crisis, depression, recovery, and then prosperity again. Though the business cycle seems to have a certain regularity over the course of many years, this, in fact, is not exactly the case.

A recent study by the National Bureau of Economic Research[3] shows that between 1855 and 1929, the longest cycle (complete from recovery to recovery) was ninety-nine months, and the shortest was of twenty-nine months' duration; also the amplitude of the cycle (that is, the heights and depths to which prosperity and depression extended) has varied considerably each time the cycle recurred.

Many economists hold that, strictly speaking, there is no one such thing as a business cycle, and to some extent they are correct because the cycle does not usually portray the movements of all businesses at any given moment. The general fluctuations of business and trade and the trends which we call the business cycle are in reality the sum total of hundreds and perhaps thousands of cycles which occur in individual businesses and industries. For instance, the building cycle runs for a period of about eighteen years from peak to peak. Copper is about eight years; sheep, nine and one third years; beef, fourteen and two thirds years; hogs, four years. Some of these individual cycles run concomitantly; others do not. When various indices of production, price, interest, etc. are superimposed upon one another, their sum total produces the general business cycle. In general, the cyclical oscillations are relatively short, and since the turn of the century the period of time which has elapsed between the peaks of each business cycle has grown shorter with each passing decade.

[3] *Bulletin* # 69, May 28, 1938.

There are other movements of price and production which cannot be considered strictly as part of the business cycle. For instance, the world-wide rise in prices, real wages, volume of production, and real income which continued through the nineteenth and twentieth centuries up to 1930 is known as the secular trend. Within this secular trend, there are, of course, the cyclical movements of business. Some other movements which are independent of cycles and secular trends, and yet which function within these movements, are the seasonal fluctuations of business and those disturbances which come from such causes as wars, floods, politics, and legislative actions, all of which are so often unpredictable, not only in their nature, but in their consequences as well.

Some price movements are rapid, and some are slow. When the prices of certain goods tend to follow the prices of goods which move more rapidly, the former prices are said to lag. Retail prices lag behind wholesale; consumers' goods, behind producers' goods; and manufactured goods, behind raw materials. Indeed, the entire cyclical picture is complicated to the extreme. Just how our nearly stabilized population and highly mechanized methods of production (which we did not have to consider up to fifteen years ago) will affect the secular trend and business cycle in the future, no one can say. We do know, however, that the future is fraught with uncertainty; we know that we cannot even attempt to measure the future beyond a period of a very few years, if, indeed, even that is at all possible; and, furthermore, we do know that the complexities of modern civilization have made the future (from a business standpoint) more uncertain than it ever was before.

Cyclical variations in business are in themselves nothing new. During the nineteenth century, depressions occurred more or less regularly, and crises occurred in 1825, 1837, 1847, and 1857. Then the Civil War interrupted, and after the war there were crises in 1873, 1884, and 1893. Since the turn of the century, however, the cyclical movements have been much shorter in their duration and in recent years have run from twenty-nine to sixty-three months.

Since the World War, price movements and long-term trends have become confused to such an extent that it is difficult for even the best trend economists to analyze them. One of the best analyses in this regard was made by Sir Walter T. Layton and Geoffrey Crother, who stated:

> "In the long stable era of the nineteenth century, price movements were so gradual that it was possible to have reasonably prosperous years even when the price-level was tending to fall. But in the post-war world, price movements have been so rapid and so extensive that the long period movement and the short cyclical movement have been merged into one swift cataclysm. The movement of prices has not been a factor in the background, making good years better and bad years moderate, or good years not so good and bad years moderate, or good years not so good and bad years worse; it has devastated the economic world and made many forms of business enterprise a matter of guessing at future prices rather than one of enterprise and hard work.
>
> "In these circumstances, to explain the (monetary) causes of price movements is a far more complicated task. It is no longer possible to ignore the waves and concentrate on expounding the nature of the tides, for the waves have mounted so high that the tides are no longer perceptible."[4]

RELATION OF CYCLES TO VALUE

In the past, fluctuations of the business cycle were not as important to us as they are today. As has been stated, there was an upward secular trend which continued unabated for almost two hundred years. Indeed, up to ten years ago land values in

[4]Sir Walter T. Layton and Geoffrey Crother, *An Introduction to the Study of Prices* (3rd ed.; London: MacMillan Co., 1938), p. 58.

the United States rose, practically without pause, along the secular line for almost two hundred years. Valuation upon the basis of forecasting permitted a large margin of error on the side of optimism; today, however, it seems very unlikely that unearned increments will continue—in fact, a large number of economists hold to the theory that the secular trend has changed its direction and is now headed downward, which would give us a future in which unearned decrements would be the rule and not the exception.

Due to the intensiveness of farm cultivation and newly developed techniques in building construction, we do not need as much land per capita as we did formerly. Also, not only in this nation, but on a large portion of the earth's surface, the birth rate is decreasing—and the population may even soon start to decline. Moreover, a fine web of economic nerves has been spun over the business and social life of the nation, so that disturbances are immediately carried from one section to another and from one industry to another almost instantly. For instance, a strike in a body plant will not only tie up the entire automobile industry, but immediately will affect realty values in those cities where such disturbances occur. Therefore, the fluctuations of the business cycle are much more important to us now than they have been heretofore.

In general, prices — and resultantly values — are high when business is considered good and production is at a high rate. As opposed to this, prices are low when business declines and production and consumption are at a low rate. FIGURE I portrays business activity in the United States from 1856 to 1939, as well as wholesale commodity prices, stock prices, and the interest rate for bonds and commercial paper.

A study of the business cycle will further reveal that, while past earnings may be a *guide* to future earnings, they cannot be the *measure* of future earnings. Past earnings are water under the bridge; if they are worthy of any consideration, it is merely that of probative significance.

The dangers involved in projecting income may be gleaned through some of the research projects of the Department of Agriculture. Prior to the World War the value of midwestern farms meant their capitalized current income plus capitalized increased future earnings, with the same rate of capitalization being applied to both present and estimated future income. What happened to a great many financial institutions as a result of lending policies predicated upon that thesis is now history; collapse and bankruptcy eventually ensued in many cases.

Not only are there many dangers confronting the appraiser who projects income at a stabilized rate from the standpoint of the business cycle; there is also the mathematical aspect, upon which Prof. Bonbright makes the following statement:

> "With most enterprises—those of a decadent type no less than those of an expanding type—any assumption that the future earnings will be stabilized at a fixed amount per year is absurd on its face. This fact would seem to preclude the capitalization of any single estimate of annual earnings and to require the separate discounting of a whole series of estimated earnings. With enterprises of a short life expectancy, such as single-mine ventures, the latter procedure is often adopted. But with enterprises of an indefinite life expectancy, much cruder methods of capitalization are resorted to. As a rule, a purely fictitious 'typical' annual earning power is assumed. Where an upward trend is anticipated, the 'typical earnings' are set higher than those expected for the next few years, but lower than those expected in the more distant future. Thus the appraiser converts an expected series of unequal earnings into the valuational equivalent of a perpetual annuity. The crudeness of this conversion is apparent."[5]

FIGURE II illustrates the simplified busi-

[5] James C. Bonbright, *The Valuation of Property* (1st ed.; New York: McGraw-Hill Book Co., Inc., 1937), I, 261.

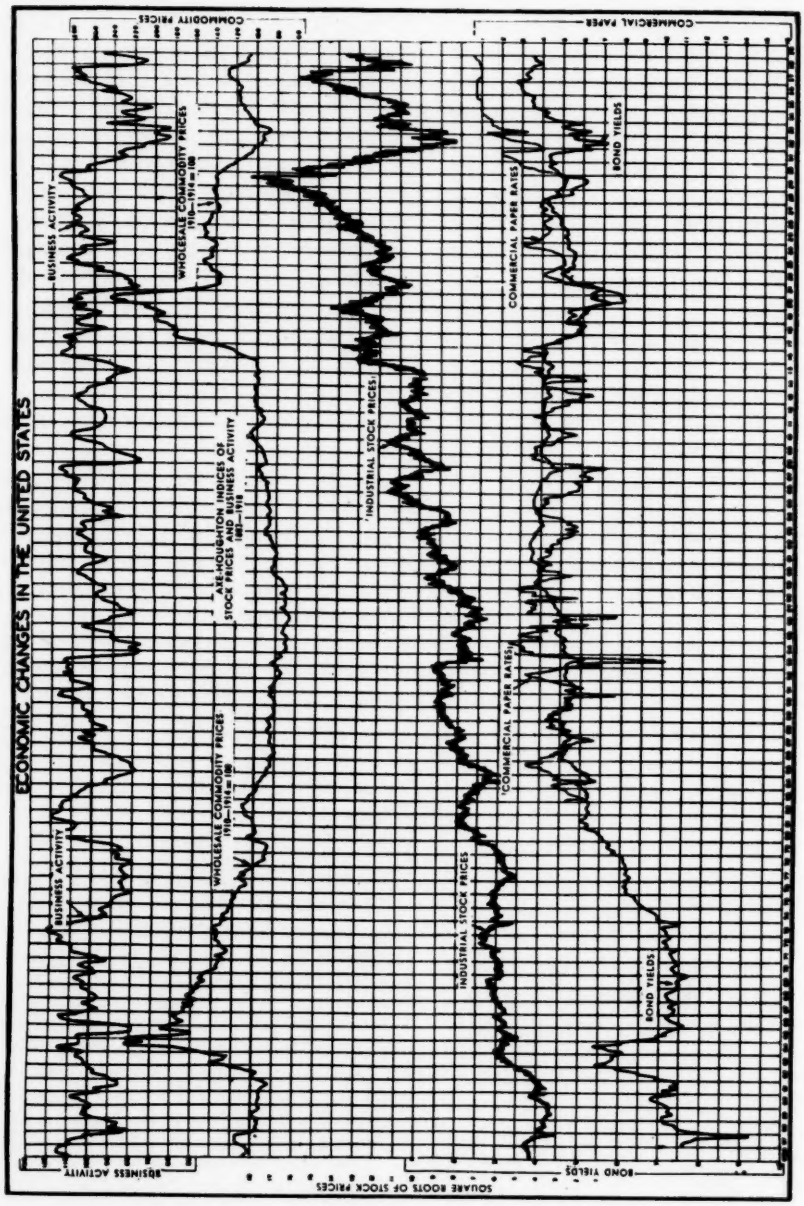


FIGURE I

(Reproduced from *The Annalist*, January 25, 1939, by permission to the author.)

ness cycle. If point A represents the time at which a valuation is desired, and current income is the basis of value, undervaluation will result as the cycle is starting on the upturn. If point B represents the time of valuation, property will be overvalued as a depression is about to commence.

In reality the cycle of construction and real estate values presents a far more complicated picture, as can be seen by FIGURES III and IV, wherein it may be noted that the time series are most irregular.

Inasmuch as capitalization depends upon forecasting, it may readily be realized that the general trend, not only of the business cycle, but of the real estate cycle, must be studied with care before any projection of income can be made. It is a well-known fact that prices and values are higher at the peak of any cycle than they are at the bottom, but the difficulty we encounter is that no one to date has been able to forecast cyclical oscillations from the time standpoint with even a reasonable degree of accuracy. However, unless an appraiser is able to project his anticipated income for at least a short period of time, his appraisal, in so far as it reflects the present worth of future benefits, fails utterly.

Dr. Thorstein B. Veblen has pointed out that "prosperity, crisis and depression are primarily the phenomena of price disturbance. . . . They affect industry because industry is managed on a business footing, in terms of price and for the sake of profits."

Dr. Wesley C. Mitchell, in his *Business Cycles*, has admirably condensed Veblen's theory in the following words:

> "This sequence of growing demand, rising prices, increasing expectations of profit, swelling capitalization of business enterprises, and expanding credit keeps repeating itself on an ever growing scale so long as its basis lasts—an anticipated increase in demand of selling prices greater than the anticipated increase in costs. But eventually the process undermines its basis. For the expense of doing business rises with the increasing cost of labor, and with the gradual extension of the advance in prices to all the commodities which business enterprises buy. In the end, these costs gain so much upon prospective selling prices as to narrow the anticipated margins of profit. Then the enhanced market capitalization of the business enterprises begins to seem excessive. Consequently, the security behind the loans which have been granted shrinks in the estimation of the business community, and ceases to be regarded as an adequate guarantee of repayment. The confident tone of business expectations which characterized the period of prosperity yields to nervousness. To bring on a general crisis, it needs but that some considerable creditor should conclude that the present earning capacity of his debtors no longer warrants the capitalization upon which their collateral is appraised. When this happens liquidation begins, extending from one industry to another and converting prosperity into depression."[6]

The movements of the long-term construction cycle and the short-term residential cycle are shown in Figures III and IV. The minor residential cycle is but one element of the major building cycle; nonetheless, its trends are most interesting. Inasmuch as real estate values and construction trends seem to be sympathetic, there might be a clue to the forecasting of the future through this medium, although it is the writer's opinion that construction lags behind the trend of real estate prices and values.

PROPHECY

All of us are given to prophecy. America's bywords only a decade ago were, "Don't sell America short," and "Two cars in every garage." Today, though we are more aware of the problems facing us, we nevertheless base every action of our business and home lives upon the future. But how little we know of the economic forces is portrayed by the fact

[6] Wesley C. Mitchell, *Business Cycles* (New York: National Bureau of Economic Research, Inc., 1928), p. 43.

(Reproduced from *The Annalist*, January 26, 1938, by permission of the author.)

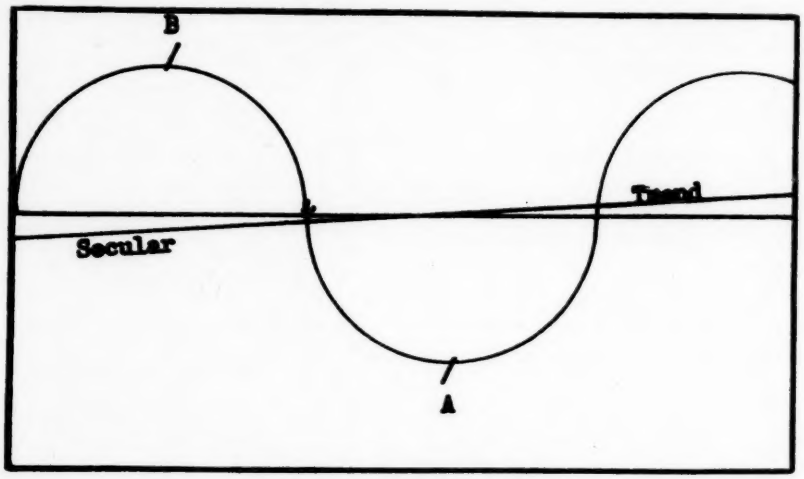


FIGURE II Simplified Cycle

that after the 1937-1938 recession, few knew that the rise of late 1938 was to come until the statistics themselves revealed the upturn.

Theories relating to the periodicity of business cycles have been as many as the rings around Saturn, and, unfortunately, just about as useful in acting as a guide to forecasting the future. Various economists have evolved a number of theories: W. Stanley Jevens, for instance, claimed a definite relation between solar activity (sunspots) and production of crops; Dr. Wesley C. Mitchell leans towards self-generation; and other theories lay greatest weight respectively on maldistribution, overproduction, and underconsumption as the cause of economic fluctuations.

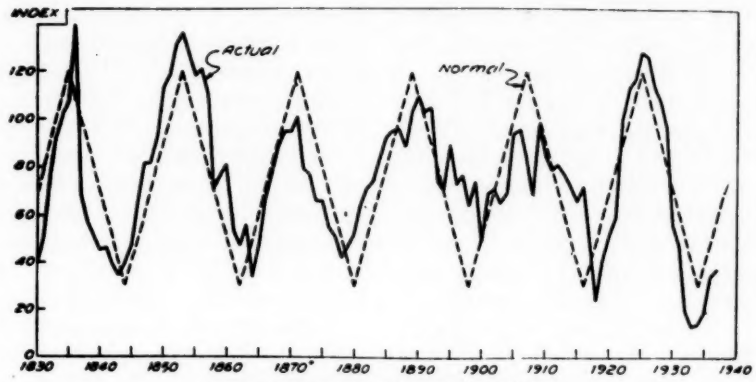
It is true that great strides have been made during recent years toward an understanding of the business cycle, but each group of economists holds to its own particular theory, with none being able to do more than explain why the last rise or decline occurred.

Difficult as may be any estimation of the future, capitalization requires that such an estimate be made. The courts have recognized this fact, and in the case of *Ithaca Trust Co.* v. *United States*, 279 U. S. 151 (1929), Justice Oliver Wendell Holmes stated, "The value of property as of a certain date, like all values, as the word is used in law . . . . depends largely on more or less certain prophecies of the future, and the value is no less real at that time if the later prophecy turns out to be false than when it comes out true."

PSYCHIC INCOME

There are two kinds of income which a person may receive — the objective and subjective, or the physical and psychical. If a property returns a certain number of dollars annually, that is physical income. That kind of income may be measured and even capitalized.

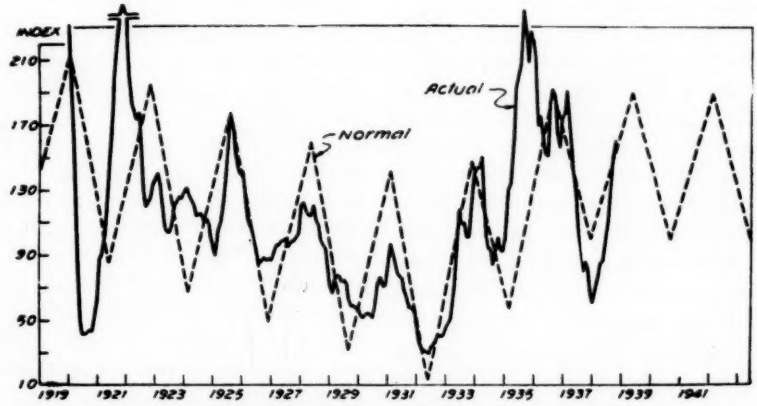
However, a type of income termed psychic cannot always be measured by the objective — for instance, the pleasure of viewing a beautiful painting. Also, men frequently hold positions, such as public office, for which they accept salaries far less in amount than they would be paid in any other pursuit. They receive psychic income in public adulation and in the es-



THE MAJOR BUILDING CYCLE, 1830-1937

The peaks in actual construction average eighteen years apart; and the low points, eighteen years. The broken line represents a normal cycle of regular timing and amplitude, eighteen years long.

FIGURE III



THE MINOR RESIDENTIAL BUILDING CYCLE, 1919-1938

The minor cycle in residential building averages thirty-three months from peak to peak. The broken line represents a normal cycle of regular timing.

FIGURE IV

(Figures III and IV are reproduced from the February 1939 Bulletin, *Farm Economics*, New York State College of Agriculture, Cornell University.)

teem in which they are held by their fellow men.

Some economists hold that psychic and physical income are equal to each other — for instance, a pound of meat which costs twenty cents produces twenty cents worth of services to the purchaser and also gives that amount of satisfaction. Irving Fisher gives the example of the musical concert for which an admission of one dollar is paid for the musicians' labor in order to give enjoyment from the vibra-

tions heard in the form of psychic income to the person paying the dollar. Dr. Frank A. Fetter[7] mentions the example of the family who may choose to live in a small house in a good neighborhood, though the rent may be the same (or even more) than for a better and larger house in a neighborhood with a lower rating. We all purchase psychic income in return for our neighbors, schools, environment, and a thousand and one conveniences.

Most purchasers of real estate pay a certain price, not only for a measurable income, but for other advantages. Historically, public opinion has always held the property owner in higher esteem than the nonproperty owner. Even today, in a small town adjoining the city limits of New York, actually only the holders of real estate in the town are permitted to vote for fire commissioners. Those who are merely rent payers have no vote.

During recent years the realty market has been greatly influenced by the fear of inflation—i.e., that money may be worth less at a future date than it is at present. In this instance, a price in excess of a normal capitalization is not paid for a present satisfaction; it is paid for the avoidance of possible, remote future, unpleasant experiences. It is not difficult to see that if $3.00 is paid for admission to a football game, the satisfaction of seeing the game cannot be capitalized at 4, 6, or 8 per cent. In the same sense we cannot measure by capitalization the fear of inflation or the satisfaction procured through the avoidance of unpleasant experiences if monetary inflation should come.

Bonbright mentions this in his recent treatise on valuation: "One aspect of this problem of psychic income, however, may concern an appraiser or a court: the effect of so-called nonpecuniary considerations on the value of property that is being appraised *primarily* by reference to its money-yielding power."[8]

The writer recently raised the question if, in valuing income-producing property, a rate as low as the mortgage interest rate could be adopted. The unanimous opinion was "no," but that answer is not convincing. The writer contends that the present realty market is now reflecting a positive and a negative rate of interest and that in the capitalization picture we must show due regard for an investment made to avoid loss as well as investment to obtain profit.

THE INTEREST RATE

The interest rate used in capitalization is the measuring rod of desires for present and future income. As a common denominator it gauges the psychological forces of future expectancies, and resultantly it becomes the balance on which the future may be weighed in the light of the present.

Considering real estate as a speculative investment, there are certain axiomatic principles which apply to all speculative investment. One is that the speculative yield must be higher than a safe yield, and another is that the speculative yield must contain an allowance for the possible loss of capital and interest. Therefore, in the speculative rate there enters what amounts to an insurance premium against loss.

Also, there must enter into the yield an allowance for management, plus a compensation for successful investment, if no loss occurs. These, then, are but a few of the elements which go to make up a speculative interest rate. How important is the choice of a rate can easily be seen when it is considered that an error of only 1 per cent can change the amount of an estimated value by as much as 15 per cent.

[7] Fetter, *Economic Principles*, Chap. 3.

[8] Bonbright, *The Valuation of Property*, I, 219.

Inasmuch as risk is the most important element entering into rate determination, it might be well to consider some of the risk elements affecting the income and the return of capital. These elements might be termed internal variables inasmuch as they arise in the operation of all income-producing real estate. They must be considered as part of the interest rate, particularly if a stabilized income is used. For the sake of clarity they are numbered—but not necessarily in the order of their importance. They are as follows:

1. *Income variables*: It is a fact that rentals of specific properties vary from year to year. A variance of 5 per cent to 10 per cent in gross income will oftentimes have great effect upon net income which is available inasmuch as the operating charges do not tend to vary as rapidly as does income. Not only do local conditions affect gross income, but general business conditions have a great effect on it also. Though there are times when a future trend of rental income can be anticipated with reasonable accuracy, nevertheless, experience has proved, at least during the last fifteen years, that the income has oftentimes been an unpredictable element.
2. *Operating variables*: Recent trends in our economic system have made operating charges most difficult to measure. Throughout the depression, the one item which no one expected particularly to increase in cost was labor. Furthermore, the cost of goods and services purchased in the operation of property does change considerably, though not as violently as does income.
3. *Fixed charge variables*: Taxes, water, and insurance change considerably over periods even as short as a year. While the cost of water and insurance remains relatively stable, taxes have been mounting steadily, and, though general opinion is that taxes will increase in the future, no one can say how much.
4. *Capital expense variables*: Over a course of years, there has been a trend wherein the owners of property have had to incur considerable expense for items such as refrigeration, radiator covers, and others which were unheard of fifteen years ago. The services which owners have had to supply to tenants—services involving capital expenditures—have increased, and this item indeed may be said to be as totally unpredictable as was the advent of the electrical refrigerator unpredictable fifteen years ago.
5. *Adaptability of improvement variable*: We are living in an era of economic change and of style change as well. Today's demands may not be the demands of tomorrow, and this fact creates a definite instability of value. The size of families is undergoing serious change, and we must realize that modes of living change as well. For instance, during the nineteen-twenties a great many apartment buildings, having apartments of from eight to twenty rooms in size, were erected in New York. Both apartment houses and hotels were built to cater to those who could pay from $700 to $1,200 per room per annum. So it may well be asked, "Is it possible to predict how adaptable any improvement will be at a certain date in the light of our experiences during the past twenty-five years?"

Truly, the task of measuring a speculative interest rate may seem well nigh insurmountable. Though the universal custom of appraisers is to combine both the safe and speculative rates, Bonbright has seriously questioned this practice. He uses the illustration of an expected stable income of $100,000 per annum. If a presumably safe interest rate of 4 per cent could be allowed and there were one chance out of ten of nonrealization of any earnings, the exact rate arrived at would be 4.44, which, it is pointed out, would hardly be hit upon by any appraiser except by accident. There is little doubt that more care is needed in measuring risk.

However, in addition to the income risk factor, there is also the capital risk factor. This, in the case of real estate, is all-important — probably more important than the safe-interest consideration.

According to Fetter, "the practice of counting the capital as equal to a fixed sum of money has suggested to some the idea that capital is, in its very nature, a permanent quantity of value. But this is

an illusion, for the 'sum of value' may be both increased and diminished, and may be utterly swept away. Capital is no more than a bookkeeping expression of the present worth of a person's control over income, definite at the moment that the first investment has been made, and thereafter merely an estimate, until the property is sold again at a price."

It is when the return of capital probability is added to the safe rate of interest plus the interest risk factor that the combined interest rate rises to a high mark. The following example is given:

Safe base rate	4.00%
Interest risk rate	0.44%
Capital risk rate:	
Possible loss of 30% of capital; capital risk spread over 20-year period = 1½% annually	1.50%
Liquidity of capital factor	1.00%
	6.94%

The choice of the above factors is subject to argument, of course, but they are not supposed to represent any particular case; rather, they are outlined in order to show the difficulties involved. The most interesting feature is that a 30 per cent risk factor for capital (which does not seem unreasonable) raises the interest rate by 1½ per cent—a very large amount.

INTEREST RATES AND PRICES

The relation between prices or values and interest rates deserves mention at this point. In general, there has been a high correlation between the two, for when prices rise, interest rates tend to rise; when prices fall, interest rates fall also. John Maynard Keynes calls this relationship, which is termed the "Gibson Paradox," one of the most completely established empirical facts within the whole field of quantitative economies.[9]

Economists generally agree that interest rates and prices tend to move together, though they are still in disagreement as to the causes. However, this need not be of particular concern at the present moment inasmuch as we are interested primarily in the effect of this correlation on capitalization procedure.

At this point it must again be repeated that capitalization relies upon the measurement of future income and a properly chosen interest rate. However, if it is future income which must be used, then we must also project ourselves into the future in our choice of interest rates. Should the future worth of income be less when it is received because interest rates have risen, then it stands to reason that the present worth of that future income will also be less if we judge the future according to future interest rates rather than upon the basis of today's lower interest.

An example is perhaps the best way of illustrating the problem. A, B, and C are predicated upon three separate assumptions:

A.	Present income $6,000 Present interest rate 6% Value	$100,000
B.	Income $6,000; rising to $8,000; stabilized at $7,000 Present interest rate 6% Value	$116,666
C.	If interest rates and income both increase (which usually occurs): Present income $6,000; rising to $8,000; stabilized at $7,000 Present interest 6%; rising probably to 7%; stabilized at 6½% Value	$107,692

Here is a problem to which we have given little attention. As can be seen, the results give a difference of over 8 per cent between B and C in computing the present value. Therefore, it would seem that not only must capitalization be approached from aspects of future income, but from future interest rates as well.

Theoretically, and probably actually,

[9] John Maynard Keynes, *A Treatise on Money* (New York: Harcourt Brace & Co., 1930), II.

there are nine variables which must be considered. They are:

INCOME	INTEREST RATES
Present	Present
Present	Increasing
Present	Decreasing
Increasing	Increasing
Increasing	Decreasing
Decreasing	Increasing
Decreasing	Decreasing
Increasing	Present
Decreasing	Present

Perhaps the whole question of capitalization may be considered difficult enough without introducing new complications into the picture. However, it must be realized that interest rates, both real and actual, are changing daily and that the appraiser must be cognizant of the trends. The following tables portray interest changes which have occurred in various types of investments during the past few years:

	1934	1935	1936	1937
Federal	2.96	2.55	2.57	2.57
State and local	4.48	4.39	4.26	4.16
Railway	4.59	4.60	4.55	4.55
Industrial	5.60	5.55	5.42	5.28
Public utility	5.09	4.99	4.86	4.71
Farm mortgage	5.78	5.33	5.25	5.25
Urban mortgage	6.30	6.10	6.00	5.90

Between December, 1937, and December, 1938, a twelve months' period, in general, interest rates dropped considerably and were as follows:

Bank rates to customers	2.45 to 2.33
Bond yields Aaa	3.24 to 3.10
Bond yields Baa	5.82 to 5.23
Bankers' acceptances	7/16 to 7/16
Commercial paper—	
4-6 months	1 to 5/8
Treasury loans —	
91 days' yield	.09 to .04
Treasury notes —	
3 to 5 years	1.31 to .71

A word of caution perhaps should be mentioned at this point. Too great weight should not be given to the short-term interest rate as is evidenced by bankers' acceptances, commercial paper, and all short-term loans. This type of debt, while considerable, represents but a fraction of the nation's total debt and is, moreover, subject to totally different factors and considerations than is the long-term debt. In general, interest rates are at the lowest point they have ever reached in the history of this country, and it would seem that from now on the trend might be upward. However, attention is called to the changing rate of interest shown in FIGURE I. It will be noted that the secular trend has been downward since 1856.

CONCLUSION

One more thought. In any discussion of the merits and demerits of capitalization, neither the proponents nor the opponents can argue with apocalyptic finality. We approach, in our value discussions, the realm of metaphysics; and perhaps it is unfortunate that the principles of philosophy, by inductive and deductive reasoning, must be applied to mundane, everyday problems in which a decision in terms of money must be reached.

What must be borne in mind is the fact that a value is an estimate; it never is and never can be a fact. The tools with which an appraiser must pursue his profession are still pitiably few; and we must realize that when we use capitalization, we are accepting and predicating our formulas not on mathematical postulates but on hypotheses and debatable assumptions. Capitalization is the safest and surest method of valuation which we have as yet found; it gives *an* answer, but never *the* answer.

The appraiser has not yet been born who can be absolutely sure, for only pagans can be sure. They need no guidance. Each, unto himself, is a Zarathustra reincarnate.

The arguments presented here are not to be thought of as right or wrong. To

repeat, they in themselves are ever-debatable assumptions. But it is hoped that they may stimulate further thought in this great field of economics, for we have to date little more than a few *obiter dicta* relating to capitalization in all the economic treatises which have been published up to the present time.

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INSURANCE COMPANIES LOOK AT APPRAISALS

PATRICK H. CLARK, M.A.I., C.P.M.

MUCH has been written concerning the theories and practice of appraising, but little on the attitude of the mortgage loan official toward the reports that result therefrom. This article proposes to show a cross section of the opinions of a number of insurance officials on this subject. The thought originated recently when I came upon a loan official deep in the task of ferreting out the whys and wherefores of an appraisal report. I asked him if he ever got lost in the labyrinth of reasoning, or lack of it, in the average appraisal. "No," he said, "but sometimes I feel like Daniel Boone when someone asked him if he ever got lost in the woods. Daniel replied, 'No, I ain't never been *lost*, but I was *perplexed* for three days once't.' " An admission of perplexity is usually a healthy sign.

I am sympathetic with this official's perplexity because frequently I have examined the files of a large insurance company in connection with mortgage loans which had reached the trouble stage and have been struck with the apparently casual manner in which loans had been processed for committee action. There appeared to be very little analysis of income or even of the physical property. Brief and uninformative reports seemed to be the rule, with no supporting data on the land valuation. A photograph, perhaps, of the building, but no neighborhood view, and too often a poor vantage point that failed to delineate the property adequately. Picture the chagrin of the loan officials, particularly during a depression period such as we have been through, when such loans come up for review.

What a pity that the thought processes of the appraiser are not fully transcribed into the records. The appraiser's thoughts are usually logical, I have no doubt, but if they are not entered in the report, his conclusions alone carry little weight in the cold light of analysis in later years. It must be borne in mind that appraisal reports are for the future as much as for the moment.

APPRAISER VITAL COG IN MORTGAGE LENDING SYSTEM

It is gratifying as well as reassuring to review present-day methods of lending, adopted in a fairly general way by most of the leading insurance companies, as contrasted with the uncertain methods of the past.

In the first place, there was a weeding of personnel, a striking transformation of the appraisal divisions of these same companies. They searched the country for the best appraisal talent and brought these men into their respective home offices. Instead of being a necessary evil, as heretofore, the appraiser has emerged as a vital cog in the lending system, if not, in fact, a veritable kingpin. A conscientious attempt was made to create a workable appraisal staff—in many cases, with successful results.

Next, there was a complete review of the mortgage portfolio. Loans were culled. Weak loans were ordered to foreclosure or requested to be paid off in one way or another. Previous lending methods were analyzed, competitors recognized, and their methods studied. In fact, there was a national "house cleaning."

Haphazard, hit-and-miss methods have given way gradually to a combination of a scientific and a common-sense approach to the appraisal problem. Junior members of the appraisal or reviewing staffs are encouraged to take courses of study, not-

ably those sponsored by our own Institute. Witness the number of insurance employees enrolled during the past three years in the Institute's courses at Columbia University and at The University of Chicago.

STATUS OF THE APPRAISER IN ENGLAND

But, while there has been improvement, we are still in the "muddling-through" state in this country, from an appraisal standpoint, as compared with what our British cousins are doing and have been doing for the past hundred years or so. Over there the independent appraisal report really means something. The appraisal profession has come of age. To become an appraiser, the neophyte first enrolls in a special real estate course at one of the leading universities.[1] After two or more years, an examination is given; then he is articled as an apprentice to a well-established broker or appraiser for another two or more years, when a progressive examination is given. If he is successful, he then is eligible for employment with some firm, but not until he joins one of the societies is he recognized by the public as an appraiser.

To become a professional appraiser in England requires long years of preparation. Should a beginner be unable to attend a college real estate course, he can take a correspondence course sponsored by one of the leading societies, while articled, during which he can pass his progressive examination, and, after serving his required apprenticeship, he then will be eligible for membership in one of the professional societies.

Two of these societies are: The Chartered Surveyors' Institution, an organization of an international character to foster ideals and progressive education in appraisal work, and the Incorporated Society of Auctioneers and Landed Property Agents—neither one of which is an exact parallel to our own Institute, yet is similar in some respects. Entrance requirements are very strict, and standards are extremely rigid. Their sphere is a bit broader than our own. Each society has a benevolent fund for less fortunate members, and the social angle is stressed.

Maurice Reidy, M.A.I., of Worcester, Massachusetts, who traveled in England recently, was asked to contact an official of The Chartered Surveyors' Institution and endeavor to secure answers for me to several pertinent questions:

"Do insurance companies depend on the society in the matter of appraisals, or do they maintain their own staff of appraisers?"

"Do these appraisers receive a fee, or do they have a retainer for year-round service?"

"Are appraisals submitted in the form of a brief or in skeleton form?"

Mr. Reidy received the following reply from Major A. H. Killick, of London:

> "Insurance companies and building societies in this country, both of which organizations make advances on security of mortgages on property, adopt both alternatives referred to in your letter. The Prudential Assurance Company, for example, which is one of the largest, have a large permanent staff of Chartered Surveyors. The Abbey Road Building Society, another very large organization, also have a large permanent staff of appraisers (or valuers as they are called in this country). Other insurance companies and building societies instruct individual firms of practitioners to make appraisals or valuations of property on which they propose to lend money, and pay them a fee for doing so. Each insurance com-

[1]The College of Estate Management, 35, Lincoln's Inn Fields, London, is controlled by The Chartered Surveyors' Institution, the Auctioneers' and Estate Agents' Institute, and the Land Agents' Society.

"In this way the education of those about to enter the Profession and become members of the Profession and become members of the Institutions is directly under the guidance of the Profession itself.

"Under the terms of its Royal Charter the College provides training for students in all matters connected with the management, admeasurement, valuation, development and any other dealing in or with land and other property. It prepares candidates for a large number of examinations held by the various Professional Institutions and also for the degree of Bachelor of Science in Estate Management of the University of London."—From the 1938 Catalog published by The College of Estate Management.

pany or building society has a scale of fees which it pays for this work. It is not usual to pay a retainer in the sense you mean; but quite often Chartered Surveyors are appointed as directors of insurance companies and building societies (the latter particularly), and receive a salary as such. They are private practitioners and would attend weekly or fortnightly board meetings, and they are not permanent officials of the building society or insurance company.

"Where a private firm is instructed to make an appraisal or valuation, it is submitted in the form of a report on the situation, condition and other factors affecting the property, written on the firm's note paper. The report concludes with the surveyor's opinion as to the value of the property."

For these and other reasons, weight is attached to the appraisal report of an English surveyor or appraiser. The appraiser has professional standing and dignity. *It is a violation of the English code for any bank or life insurance company in England to loan money on real estate without employing an outside appraiser as well as its own salaried staff.* Not only is weight attached to the findings of these valuators, but there is a very definite responsibility. The appraiser is criminally and civilly liable for his mistakes.

Bracton Goldstone, M.A.I., of New York City, cites a case which occurred in London recently in which an appraiser valued a building, but failed to state in his report that the roof was in poor condition and should be repaired. Naturally, he failed to state the cost of such repairs. The purchaser, when the omission was discovered, sued the appraiser and recovered.

The attitude of English lending institutions, whether they be insurance companies or building and loan societies—which, by the way, are a larger factor in the mortgage loan field than insurance companies—is one of respect for the appraiser, each being dependent largely upon the other.

In sharp contrast, here in America the profession of appraising is still in the probation period; it is still viewed with distrust and misgiving in some quarters; and the appraiser is neither allowed nor required to assume any legal responsibility as yet. These attitudes exist in spite of the fact that appraisals and appraisers are practically the foundation upon which the colossal mortgage loan investment business is built.

The magnitude of this business, dependent to such a large degree on the appraiser, is evidenced by the following figures: On December 31, 1937, the aggregate mortgage loan investment of 141 insurance companies in the United States totaled approximately $5,330,000,000, or over twice the funded debt of New York City. Twenty-five leading life insurance companies held $3,623,000,000 of this amount. In addition to the mortgage loan investment, there was held in the form of real estate acquired the vast sum of $2,252,000,000. The twenty-five leading companies held over 90 per cent of this sum. The total value of real estate owned by these insurance companies today would have been sufficient to have wiped out the gross national debt of 1916, with more than a billion dollars left over.

WHAT INSURANCE COMPANIES THINK OF THE APPRAISER

To find out the attitude of the mortgage loan officials toward appraisers and appraisals, questionnaires were sent to the mortgage loan officials of a large number of insurance companies; they were sent to both large and small companies in order to obtain a fair cross section of prevailing opinions. The response was prompt and cordial.

The questions can be divided, roughly, into three groups. Group I was to determine the prevailing source of appraisals; Group II was to determine the basis of

analysis, or what the lending officials look for in these appraisals; and Group III was to determine just how the appraisal profession stands in the estimation of these officials.

Naturally there was a division of opinion on most of the questions, but there was also a fairly common ground upon which they all met—that is, a sincere desire to *prove* the *worth* of the security upon which a loan is based. The approach was varied, but toward a common goal.

Question Group I was phrased thus: In the appraisal of city property for mortgage loans do you depend entirely upon outside independent appraisers, upon appraisals furnished by your correspondents, or appraisals made by your own salaried staffs?

Strange as it may seem, only 55 per cent of the group use outside independent appraisers and some only in rare cases. Forty-five per cent do not use independent appraisals at all, whereas none of the group relies entirely upon correspondent appraisals. Sixty per cent of the group have great reliance upon their salaried staff, whereas only 16 per cent rely entirely upon this source. Twenty-three per cent have great reliance upon correspondent appraisals, but bolstered by their salaried staff. Of the 55 per cent using independent appraisers, only 11 per cent depend entirely upon this source; 5 per cent use a combination of all three.

From these figures, it appears that a majority of institutions use a combination of salaried staff and independent appraisers, with the weight on the side of their salaried staff.

The plan of using a salaried staff in the majority of cases has considerable merit where this staff is thoroughly trained and qualified. But unfortunately one hears stories like the "classic" that came to my attention recently, wherein a real estate appraiser on the salaried staff of a large lending institution is reported to have made twenty-two appraisals in one day on property scattered in different parts of New York City! I submit that no one can do justice to that many properties in that length of time.

Another incident was noted wherein an application for a sizable loan was investigated by a member of the salaried staff of a large insurance company who had never before seen the town in which the property was located except through a car window. The investigation lasted three-quarters of an hour; three people who were not competent to pass judgment on the project were interviewed. A hasty negative report was submitted, and the company lost a valuable investment to a rival institution which took pains to have a thorough investigation made by a trained man who knew the territory.

A good appraiser saves many times a year what he costs his principal, whether he is upon a fee basis or a salary basis. However, it is gratifying to note, generally speaking, that the caliber of the salaried appraiser in these institutions is improving. But there is a long way yet to go. Character cannot be bought, and ability in the long run must be paid for in coin of the realm. Furthermore, there is the slow but definitely increasing demand for independent and disinterested appraisals both on the part of regulatory authorities and of the public.

The second group of questions asked: In reviewing appraisals in connection with loans submitted to your home office, do you place more reliance upon the logical analysis of the data tending to establish the probable market price of the property, upon depreciated replacement cost, upon capitalization of the expected income, or upon your confidence in the judgment of the appraiser?

The replies were a bit more uniform than for Group I. Seventy per cent base their

review of appraisals upon the capitalization of the expected net income where *income properties* are concerned; 85 per cent rely upon the analysis of market prices for *dwellings*. Twenty-three per cent rely principally upon the judgment of the appraiser, whether he is an independent appraiser, correspondent, or one of the salaried staff; and 5 per cent rely upon depreciated replacement cost for both *income* and *dwelling* properties, with an eye to trends in land value. It was interesting to note replies such as: "We do not believe blindly in the appraiser's valuation in any case"; "Repose absolute confidence in judgment of salaried staff. Independent or local appraiser is invariably optimistic"; "Great dependence upon judgment of appraiser, with recognition of other factors incurred"; "Capitalization of expected income, but above all, confidence in judgment of appraisers."

It may be gathered from these figures that the scientific approach to appraisals is gaining ground rapidly with insurance companies, but that the judgment of the appraiser is the keystone in the formula. This brings us to the last group of questions, which strike home to those of us in the profession.

The question ran like this: Do you believe the aroused interest in appraising as a profession, in organized appraisal groups during the past few years, has improved appraisal standards, or has it tended to a more theoretical technique to the exclusion of practical judgment?

A large number of "yes—but" answers were received. Seventy per cent of the institutions believe that organized appraisal groups have improved the appraisal standards. Twenty-three per cent believe that they have tended to a more theoretical technique to the exclusion of practical judgment. Seven per cent hedge in their attitude. An officer of one large institution stated bluntly, "Organized appraisal groups are tending to become rackets. Technique dazzles many appraisers who fail to look at the results objectively. Appraisers should not feel that they must protect themselves on past appraisals even though the conditions surrounding the property have changed." And another, "Broadly speaking they (the groups) are excellent but 'too much learning is a dangerous thing.' Common sense is the key to the appraisal approach." And again, "It has improved standards, but the appraiser tends to emphasize theory . . . ." On the other hand we have, "It tends to more theoretical technique but not to the exclusion of practical judgment—techniques have tended to *aid* good judgment rather than for any other reason. It has raised the standards." But, "As a whole . . . . has improved the standards but appraisal formulae lean too much to theoretical technique and better results could be obtained from sound judgment of an experienced appraiser who keeps himself informed of procedures of organized appraisal groups." Thus, all down the line.

Does this mean that our graphs and imposing formulae are frowned upon by the users of our service? Not at all; but it does mean that the appraiser who tries to alibi a land value by a trick formula had better be sure of his hypothesis and data.

These gentlemen who occupy splendid offices and pay our fees are no "stuffed shirts." Their criticism in some ways is well directed and pointed. The emphasis, however, is still on those lowly virtues of common sense, sound judgment, and character which have always been and will continue to be the basis of all appraising.

DEPRECIATION AND OBSOLESCENCE IN THEATRES

WILLIAM W. TANNEY, M.A.I.

THEATRE buildings present an interesting field for the study of obsolescence and depreciation. Like all special-purpose buildings, they are particularly vulnerable to changes in neighborhoods and trends in public habits, but changes in the theatrical business itself and new developments in theatre housing have provided still other factors of obsolescence. This obsolescence is due chiefly to overcapacity in size of the buildings and to changes in the arts and sciences.

The movies, of course, created great changes in the theatrical field. That development practically eliminated stage plays and the old "opera house" in all but the very largest cities. The invention of talking pictures caused another revolution in the theatre by changing not only the form of entertainment, but also by bringing about a change in the building design for satisfactory presentation, resulting in great obsolescence even in relatively new buildings. Proper sound reception is now extremely important. This new entertainment device has drawn to the theatre music lovers and people who previously supported the legitimate stage exclusively.

In an endeavor to estimate to a reasonably definite degree the economic loss through obsolescence in some of the existing theatre buildings in Detroit, a survey of theatre locations was made covering the period from 1900 to 1938. The substance of that investigation is presented here as typical of the development and changes which are occurring in all cities.

In 1900, Detroit had a total of eight theatres — six in the downtown area and two in suburban communities which later became a part of the city. All of these presented stage performances, either drama, vaudeville, or burlesque. Of these eight theatres, only two remain today. One is a burlesque house, and the other is showing pictures. Only five of the one hundred sixty-five theatres now operating in Detroit present stage plays exclusively, and three out of the five are burlesque houses. Only one motion-picture house offers a stage show in addition to a feature film.

Moving pictures were invented about 1893 and came into general commercial use with the introduction of the nickelodeon about 1905, which increased in number until 1914. The early movie houses were usually remodeled stores. Now the nickelodeon type of theatre has been eliminated almost entirely because narrow walls cause an excessive distortion of sound.

As motion pictures grew in popular appeal, special picture houses began to be erected about 1914. Theatre construction reached a new level as the problems of this period were standardized upon a scientific basis. These theatres also presented vaudeville acts and therefore were designed with stages and all the facilities of the older stage-show houses. Many of these buildings were equipped with pipe organs to carry the tempo during the showing of pictures. During the boom days of the nineteen-twenties, bigger and better picture theatres were erected. The competition between operators extended to elaborate architectural treatment of both the exteriors and interiors of the buildings. Theatres were designed in Italian Renaissance, Egyptian, Chinese, Mayan, and many other styles. Expensive lobby and lounge furnishings and garden and fountain effects were installed to provide customers a few hours of luxurious living in a beautiful palace.

The talking picture, introduced in 1930, brought about another radical change in theatrical operation, resulting in almost complete elimination of the stage productions outside of New York and Chicago. Vaudeville acts and orchestras sought new outlets in the night clubs, taverns, and broadcasting stations. The fading of the so-called legitimate show has been due also to the high cost of personal performances.

DEPRECIATION

During the period of the thirty-eight years investigated, 343 theatres have been operated in Detroit, of which 165 are now operating, and 178 have been discontinued. In order to indicate the influence of the community theatre, the locations were divided into three groups—the downtown area (one-mile circle), within Grand Boulevard (three-mile circle), and beyond Grand Boulevard (outlying area). The section within the Boulevard (three-mile circle) was the approximate limits of the city in 1900. The increase in the number of theatres should be considered in relation to the growth of Detroit during the period. In 1900, the area of the city was 28 square miles; in 1938 it was 138 square miles. The population in 1900 was 285,000; in 1938, it was 1,750,000.

This survey, which was made to estimate the economic life of theatres in Detroit, started with a year-by-year count of all theatres which had been operated in the city, taking the information from city directories and other records for the period from 1900 to 1938. This period encompasses the entire life of all motion-picture theatres. Locations were taken as the basis for the count—that is, if the name of the theatre changed from time to time, only one theatre was reported for that location.

The following table indicates the life of theatres now operating in Detroit:

LIFE OF OPERATING THEATRES

Year of Opening	Central District One-Mile Circle	Three-Mile Circle	Outlying District	Total
1900	1	0	0	1
1901	1	0	0	1
1902	0	0	0	0
1903	0	0	0	0
1904	0	0	0	0
1905	0	0	0	0
1906	0	0	0	0
1907	1	0	0	1
1908	0	1	0	1
1909	0	1	1	2
1910	2	0	1	3
1911	0	0	2	2
1912	1	4	1	6
1913	1	3	3	7
1914	1	10	6	17
1915	0	8	9	17
1916	1	2	3	6
1917	2	2	4	8
1918	0	1	2	3
1919	0	1	3	4
1920	0	1	6	7
1921	1	1	5	7
1922	0	0	1	1
1923	0	1	5	6
1924	0	0	1	1
1925	2	2	9	13
1926	1	0	6	7
1927	2	0	6	8
1928	2	0	7	9
1929	2	0	3	5
1930	1	0	5	6
1931	0	0	2	2
1932	0	0	0	0
1933	0	2	1	3
1934	0	0	2	2
1935	0	0	2	2
1936	0	0	1	1
1937	0	0	5	5
1938	0	0	1	1
Total theatres operating	22	40	103	165
Total years operating	448	903	1,643	2,994
Average years operated	20.3	22.6	15.9	18.1

Beginning with the rise of the silent film into an industry about 1914, the building of large and decorative theatres in the twenties, and then the introduction of the new type of "sound" theatre, one can visualize the peaks of development from the above table. The nickelodeons of the 1905-13 period have been almost entirely discontinued.

The location of the theatres in the outlying sections indicates the trend which carried the movies to the community. The area within the three-mile circle developed

commercially as new residential neighborhoods were developed in the outlying districts. Only two small theatres started operating in the older section since 1925.

In the downtown section, ten theatres now operating were started since 1925. Four of large seating capacity were built in conjunction with office buildings during the days of easy financing. Two others are now seldom used for any type of show. Three are small third-run houses. The other is an old auditorium converted into a theatre and is now the only one regularly playing legitimate stage shows.

There are only four theatres now operating which have a life of thirty or more years—two in the central district and two located in the three-mile section. Twenty houses have had between twenty-five and thirty years of operating life; and fifty theatres have been open from twenty to twenty-five years. How long these buildings will survive the inroads of the new sound theatre is, of course, problematical. Certainly many of them will have to meet the competition of theatres with better sound reception.

Usually theatres up to 400-seat capacity were the nickelodeon type and operated in converted store buildings; others having up to 800-seat capacity were special-type buildings with ramp floors, but of a size and shape which could be remodeled for commercial use when the demands of the location warranted; those over 800-seat capacity were strictly one-purpose structures, generally erected on the rear of the site, with almost no conversion value except in the downtown district.

LIFE RATE OF DISCONTINUED THEATRES

The investigation revealed also the life rate of those theatres which did not survive. The following table does not refer to the year operations were started, but indicates only the length of years locations existed as theatres before operations terminated:

LIFE OF THEATRES DISCONTINUED
1900-1938

Life in Years	Central District One-Mile Circle	Three-Mile Circle	Outlying District	Total
1	4	13	9	26
2	2	2	13	17
3	3	6	8	17
4	2	4	9	15
5	3	3	3	9
6	2	2	3	7
7	1	4	3	8
8	0	2	1	3
9	1	1	4	6
10	2	3	3	8
11	3	1	2	6
12	2	0	1	3
13	2	3	3	8
14	2	2	2	6
15	1	0	0	1
16	1	4	2	7
17	0	1	2	3
18	2	4	1	7
19	2	0	1	3
20	1	1	0	2
21	3	3	1	7
22	0	0	0	0
23	1	1	0	2
24	0	2	1	3
25	0	0	1	1
26	0	0	0	0
27	0	0	0	0
28	1	0	0	1
29	0	0	0	0
30	0	0	0	0
31	0	0	0	0
32	1	0	0	1
33	0	0	0	0
34	1	0	0	1
35	1	0	0	1
36	0	0	0	0
37	0	0	0	0
38	0	0	0	0
Total theatres	44	62	73	179
Total years operated	505	546	497	1,548
Average years operated	11.5	8.8	6.9	8.7

It may be observed in the list of discontinued theatres that over one half of the number (eighty-four) survived five or less years. These, for the most part, were ill-advised nickelodeons started during the early periods of rapid development of the movies (1905-14) — natural in any new type of business. Others were operated successfully over a period of years and then closed. Many of these were crowded out by the newer type of theatres or could not survive with the use of sound pictures.

Only three discontinued theatres were in operation longer than thirty years. All of these were old legitimate houses and located on high-valued land in the downtown section. Two of these buildings were razed; one was replaced by a modern commercial building, and the other site is now being used for a parking lot. The third building was converted into a department store.

The average age of 8.7 years in these discontinued theatres is rather startling. If we eliminate the theatres which were operated only 5 years or less as being temporary ventures in buildings not specifically designed as theatres, then we have ninety-five theatres which have had various lives from 6 to 35 years for a total of 1,332 years, or an average life of 14.1 years. This is still a much shorter life than we should ordinarily expect. Thus, while the discontinued theatres had an average life of only 8.7 years if all theatres were included, or 14.1 years if the temporary ventures were eliminated, the theatres still operating have a present life average of 18 years, and presumably will continue to operate for some period yet.

The downtown theatres have had an average life of 20.3 years, as compared with an average of 22.6 years for those in the three-mile circle, which comprises the older residential districts. In the more outlying areas, the average life is 15.9 years. In the older residential areas close to downtown — that is, the three-mile circle — most of the theatres now operating were built during the period from 1912 to 1920. The lack of newer theatres in this area may be explained by the fact that the older residential areas have been losing population since 1925, with the result that there is no incentive for the construction of new theatres; consequently the older ones can continue to operate.

In the outlying areas beyond the three-mile circle, the average age of the present operating theatres is 15.9 years. It will be noted that seventy-three theatres were discontinued in this area, with an average life of 6.8 years before closing. These outlying areas furnish the best example of real competition among theatres, particularly in the building type and appointments, which factor tends to cause fairly rapid obsolescence.

It will be noted from the schedule that of the 165 theatres now operating in Detroit, only 22, or about 14 per cent, are in the downtown area; 40, or 24 per cent, are in the midtown area; and 103, or 62 per cent, are in the outlying areas. In theatre seat capacity, it is estimated that the downtown area would rank about 20 per cent, the midtown area about 20 per cent, and the outlying areas about 60 per cent.

The most outstanding feature of the entire survey is the fact that of the 345 theatres which have been operated in Detroit, only 29 survived longer than 25 years; 5 of these have been closed.

The conclusion to be drawn from this study of the economic life of Detroit theatres appears to be that one should not estimate the useful life of any theatre at more than 25 years, and in many instances a much shorter period should be used; particular attention should be given to the character and development of the district in which the theatre is located. Another important factor is the adequacy of the theatre building.

OBSOLESCENCE

The general use of the talking picture created a demand for a suitable building adapted to good audition of the program. This led to the design of a type of building having radical changes in construction, in use of materials, and in decorations. The following comparison of two

existing buildings will serve as an illustration.

Theatre A was erected in 1927 during the era of silent films. Theatre B was a composite of the new theatres built in 1937 and adjusted to conform in seating capacity with Theatre A. Both theatres sell the same entertainment programs, contain the same number of seats (1,800), and have approximately the same gross income and show expense.

Theatre A was typical of the new theatres at the time it was erected. The lobby and auditorium were elaborately decorated to attract patronage and compete with other theatres of the same class. The lobby had an expensive mosaic floor costing some $20,000. The foyer contained fountains with goldfish swimming around in pools colored with a variety of lights. *Objets d'art* and statuary were recessed in the walls of the auditorium. The ceiling had a starlit effect. These expensive decorations were installed to sell the theatre to the public. It was a good investment. People talked about the beautiful theatre, and this type of advertising paid well. The $30,000 pipe organ played soothing or thunderous music to accompany the theme of the picture. Vaudeville acts were part of the show and assisted in drawing customers. The stage show, of course, required a large stage and scenery loft with gridirons, a large switchboard for lighting effects, dressing rooms, and an orchestra pit. The city fire code required a fire escape for the dressing rooms and an asbestos curtain. The heating and ventilating systems were the best known at the time of erecting the building; however, the drafty stage and a high auditorium required an excessive amount of heat.

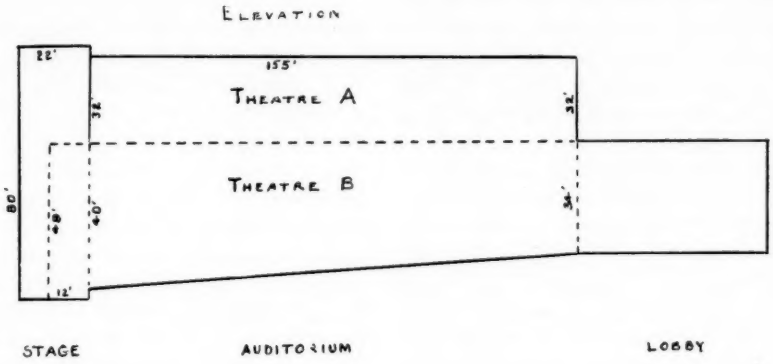
In 1931, when the silent film was outmoded, talking pictures were used exclusively in Theatre A. The vaudeville acts were discontinued, and the orchestra and pipe organ were no longer needed. The large stage and the dressing rooms were surplus space. Only a few contacts on the expensive switchboard were used; the costly lobby floor had to be covered with carpet because the noise carried into the auditorium. The elaborate decorations and ornamentations were useless as the house was dark throughout the entire performance. The plastered walls created echoes, and draperies were hung to absorb the sound.

In 1934, the first theatre to be designed especially for the talking picture was erected in Detroit. There are now seven of these new-type houses embodying the new trend in design.

Theatre B, erected in 1937 and typical of these theatres, was designed especially for the talking picture. The size of the building, as compared to Theatre A, was reduced by the elimination of the stage loft and part of the stage itself. Only sufficient room was provided for the screen and speaking apparatus. The lower ceiling added acoustical value and also effected a saving in fuel. The balcony was no longer a necessity in the average neighborhood theatre. The equipment provided only a small switchboard. The gridiron, asbestos curtain, orchestra pit, and pipe organ were eliminated. The heating and ventilating equipment had the benefit of the rapid progress made in these two industries during the past decade.

The new-type theatre is constructed of steel frame and wall-bearing masonry. The interior facings of the walls are cinder block. This material has better acoustical qualities than plastered walls. The cinder block is painted with a water paint in a simple but pleasing design. All of the features of the new theatre are of value. They not only add to the new type of entertainment, but they also save in the cost of construction.

The scale drawing shown below visualizes the difference in size between Theatres A and B.



LOSS IN VALUE DUE TO OVER-IMPROVEMENTS

Theatre A, fully equipped and ready to operate, actually cost $546,000, exclusive of land, in 1927. Without the lobby it contains approximately 1,276,000 cubic feet; it would have cost $360,000 to have reproduced the structure in 1937.

Theatre B, exclusive of the lobby, contains approximately 650,000 cubic feet and cost $110,000 to build in 1937. The loss of value in Theatre A, because of overcapacity and change in design, as well as the use of materials, was $250,000. The cheaper cinder blocks, decorated in a simple design, replaced the artistic plastered walls. The plumbing equipment in the dressing rooms was eliminated entirely. The fire escape was no longer required. Theatre B does not have large chandeliers hanging down from a high ceiling. In substance, the cubic foot cost rate was reduced from $.28 to $.17 by reduction in size, the use of new materials, and the elimination of expensive equipment.

The equipment of Theatre A, although necessary during the days of the silent film and vaudeville, has no place in the new-type "sound" theatre. The cost of some of the equipment, listed in the following tabulation, is given to demonstrate further the loss through obsolescence incurred by reason of a new invention.

Pipe organ	$20,000.00
Statuary	2,000.00
Orchestra pit, curtain, and scenery	10,000.00
Fountain and *objets d'art*	5,000.00
Total	$37,000.00

LOSSES IN THE OPERATING STATEMENT

The extra burden of operating Theatre A resulted in a reduced net income and a loss in value measured by the capitalization process. The principal losses were as follows:

	Theatre A	Theatre B	Loss in Theatre A
Taxes, building only (1938)	$8,198.00	$4,428.00	$3,770.00
Fire insurance	350.00	220.00	130.00
Fuel	2,400.00	1,000.00	1,400.00
Total			$5,300.00

If Theatre A had been encased in a vacuum-sealed enclosure the day construction was completed and opened for operation ten years later (in 1938), the losses from obsolescence would have been sustained although no wear and tear whatsoever of the structure and its equipment took place.

DEPRECIATION AND OBSOLESCENCE IN THE TAX STATEMENT

Many theatre owners have petitioned tax authorities for adequate allowance for depreciation and obsolescence. The following case of *Graeper* v. *Commission of Internal Revenue,* (1933) 27 B.T.A. 632, is cited as an example. The Board of Tax Appeals stated:

> "In his income tax return petitioner deducted 4 per cent of the cost of his theatre for depreciation. Respondent allowed only 3 per cent. Petitioner now claims 5 per cent for depreciation and obsolescence. The building is of reinforced concrete construction and should last many years, but its usefulness as a theatre will be much less than its physical life. Already the character of its patronage has deteriorated and several newer theatres have become its competitors. One witness, a real estate appraiser of experience, limits the useful life of the theatre in question to twenty years from its date of construction. He also testified that any remodeling would be impractical.
>
> "The respondent's allowance for 3 per cent deduction was apparently for depreciation only. We think there should be some allowance in respect of obsolescence. As the evidence before us indicates that the building will become useless in twenty years' time, in our opinion 5 per cent deduction to cover both depreciation and obsolescence should be allowed."

In a statement similar to that of Theatre A, the improvements are written off at the following annual rates:

Building	5%
Building equipment	4%
Electrical signs	5%
Stage equipment	10%
Booth equipment	8%
Organ	10%
Chairs	5%
Furniture	8%

Recently a theatre property located in Detroit was offered at a price of $150,000 cash. The building cost $300,000 in 1927 and is similar to Theatre A except that it is not as expensively furnished. The property includes five stores and fourteen offices. The theatre has 2,175 seats and is equipped with stage, dressing rooms, and balcony. There is no competition within two miles, and it serves a local district of some 30,000 people. The site is 120 by 195 feet and is located about 150 feet from the main street and the 100 per cent retail block. The price reflects the large loss in value due to obsolescence.

The results of obsolescence in the picture houses are nation-wide. Sooner or later nearly every theatre which was constructed during the era of the silent film will feel the effects of the "talkies" and will have to provide adequate sound reception. Ownership of theatres involves many risks — some of which are management, competition, location, neighborhood influences, policy of distributors and producers of films, adequacy of the building itself, and new methods in presenting popular entertainment. Somewhere in the future looms television. Will this new invention influence the risks of theatre ownership ten or twenty years hence by making today's theatre obsolete?

PROFESSIONAL ETHICS

HARRY GRANT ATKINSON

THE WORD "ethics" is derived from the Greek word "ethos" which carried the connotations of *rightness* and *fairness*. It implied *reason* and *foresight* in human conduct. It stressed the intellectual side of human relationship.

This concept of *rightness* has come down to us through the ages and still covers a broader field of human behavior than is encompassed by law. Being ethical is synonymous with being worthy of respect and confidence. It is one of the indispensable ingredients of professionalism. To be unethical is to be unprofessional. No vocational group can achieve or maintain a professional status unless its members are everywhere recognized as individuals who are ethical beyond question.

No appraiser who regulates his conduct solely according to what the law permits, rather than what honor and decency require, is worthy of membership in his profession. Being ethical, purely and solely for the sake of being so, is the primary obligation of the professional appraiser. It is an obligation that he owes to himself as well as to his family, his brother professional men, his clients, the public in general, and his professional society as such. The unethical appraiser cannot in his own heart have any real respect for himself. Everyone who knows the kind of man he is holds him in contempt. No one respects him.

There is a second reason why being ethical is of basic importance to the individual appraiser. That reason lies in the fact that *it pays to be ethical.* It pays to be ethical because public confidence in the appraiser's integrity is the most precious business asset he can have. Honest clients do not employ crooks to make appraisals for them; but they are willing to pay well for the services of competent men in whose integrity they can rely.

We recognize this principle of human conduct as a self-evident truth in so far as the individual is concerned. But we do not always fully appreciate the relationship between the ethics of an individual and the welfare of the professional group to which he belongs. The most serious problem which a profession has to face is that of public indignation against its individual members. For the public does not discriminate between the individual unethical member and the professional group. It is human nature to generalize. How often have we heard such expressions as, "Ever since that preacher did that thing, I have had no use for preachers," or, "I have no faith in the church because there are so many hypocrites in it," or, "You can get an expert to testify to anything"?

Thus it is that the unethical appraiser brings disrepute upon all the members of his profession indiscriminately. His actions tend to undermine public confidence in the reliability of all appraisers.

Therefore, it becomes a matter, not only of sturdy morality and personal decency, but also of public policy and professional control, to establish certain standards of conduct, to express them frankly and publicly, and to coerce all members of the organization into strict compliance with them. In a moral sense, at least, each member has a valuable property right in the good name of his profession. The organization should not permit that property right to be jeopardized or destroyed by the cancerous influence of traitors to the faith.

Rules of professional conduct fall into

four groups: (1) rules governing relationships with clients; (2) rules governing relationships with the public at large; (3) rules governing relationships with individual fellow members of the profession; and (4) rules governing relationships with the professional body as such. We shall make no attempt here to discuss any one of these four phases of professional conduct in detail, but shall consider one or two of the most significant aspects of each of them. Our interest for the moment lies in the principles upon which specific rules of conduct are based rather than in particular rules themselves.

RELATIONSHIPS WITH CLIENTS

With respect to the client, the professional man has the obligation of doing honest, faithful, and efficient work. The appraiser holds himself out as an expert, as an authority, as a workman worthy of implicit confidence. It is upon this basis that he is employed. It is for this type of service that he is paid. He has no right, therefore, to accept an assignment to appraise a property which he knows he is incompetent to evaluate. He has no right to accept an assignment which he does not expect to carry through efficiently and thoroughly. Regardless of the size of the fee, he is obligated as a professional man to give the very best service of which he is capable. To accept a fee for work which is less efficient and reliable than the client has a right to expect is to be guilty of a violation of professional standards.

The appraiser cannot excuse himself by saying that the fee was so small that he could not afford to do good work. He cannot put the responsibility for his sloppy work on his client. The responsibility is his, and his alone. The controlling principle is always and forever the single standard of being worthy of confidence. Each and every failure to measure up to this standard reflects unfavorably upon all other appraisers and is vandalism against their professional standing.

RELATIONSHIPS WITH PUBLIC

With respect to the public at large, the appraiser is under exactly the same obligation to do honest and dependable work. Purchasers of equities must rely upon his value estimates as being sound. Investors must have confidence in his integrity if they are to loan savings and trust funds upon the basis of his valuations. Taxing authorities, courts, and other governmental agencies, acting upon behalf of the people, look to the professional appraiser for unbiased and faultless work. The appraiser who fails to measure up to these expectations is guilty of betraying a public trust. His work is a fertile breeding ground for all sorts of maggots of crookedness. He deserves to be classified with the fourflusher, the quack, the shyster, the racketeer, and the thief.

That is the way he looks in the eyes of the man who relied upon his valuation, only to suffer financial loss. Such a man condemns not only the appraiser who was responsible for his loss, but he tends to lose faith in all appraisers. He has less respect for the profession as such.

The profession has the definite obligation of protecting the public against the practices of the unethical appraiser. In so doing, it protects the marketability of the services of all of its members and safeguards the dignity of the profession. This is the reason why the American Institute of Real Estate Appraisers condemns contingent fees and certain types of summation appraisals. This is one of the chief reasons behind all of the thirty rules that constitute its *Rules of Professional Ethics.*

RELATIONSHIPS WITH FELLOW MEMBERS OF THE PROFESSION

With respect to the individual fellow members of his profession, the appraiser

has the ethical responsibilities of being fair-minded, trustworthy, and constructively helpful. He also has the responsibility to his profession of insisting that each member conform strictly to the ethical principles which the group avows.

It is unethical and unprofessional for one member to originate or spread gossip about another member, to speak disparagingly about another member, to say or do anything that tends to undermine confidence in another member's ability or integrity. It is unethical and ungentlemanly to say or do any of these things, unless the member who does them is prepared to go before the Disciplinary Committee and prefer charges leading to the expulsion of the member against whom he inveighs.

No form of theft is more reprehensible than the petty larceny that lurks behind innuendoes against a professional man's reputation for competency or integrity. The man who indulges in this unethical practice seeks to steal some of the confidence which his victim enjoys and appropriate that confidence for his own. No breach of ethics is more contemptible or more foolish — for the sabotaging of another man's professional reputation invariably lowers the respect which the listener has for the individual who is committing the vandalism.

Every professional man is, in a very real sense, his brother's keeper. This is true at least to the extent of being an example of right conduct and thereby admonishing his less conscientious fellow members. And every professional organization is the keeper of its members by being obligated to the public to expel from membership all who fail to keep the faith.

RELATIONSHIPS WITH THE PROFESSIONAL BODY

With respect to the professional group as such, the appraiser has the ethical obligation of doing everything in his power to extend its strength for service and its prestige. He has the obligation also of being ruthlessly aggressive in excluding the unfit and in purging the organization of dishonest members. His profession will be impotent if it is represented by an organization that is too small, if it does not have members in all parts of the country, if there are not enough members to do the work to be done. Proper and adequate increase of membership strength is one of the vital problems of every profession.

Until a man can freely encourage the very best types of manhood and the most competent competitors in his field to enter his professional organization, he has not caught the nobler sense of professionalism. Until he can do this, he has not acquired the professional attitude. He must not only be willing but eager for every man who meets fully the standards for admission to become a member.

No profession was ever developed unless its individual members placed the welfare and the prestige of the group above their own personal interests. There is no place in a professional society for the man who wants merely to get and who will not give. Such a man is not a professional man. He is a stumbling block and a handicap to the group as a whole. He is a chiseler and a moocher. He is not entitled to the respect of his fellow members nor to any of the benefits that accrue to the title which his professional affiliation is intended to bring to him. For the professional spirit is a *co-operative* spirit dedicated to the finest ideals of quality workmanship, honest relationships, and unselfish service. The professional character cannot be bestowed by the awarding of a certificate. It must be *acquired;* and it can be acquired only by becoming the kind of a person that a professional man is.

WHAT THE ATTORNEY EXPECTS OF THE APPRAISER

ROBERT P. BUTLER*
AS TOLD TO
AUBREY MADDOCK, M.A.I., C.P.M.

INDUSTRY, intelligence, and integrity are the qualities an attorney seeks in an appraiser for eminent domain cases. This branch of appraisal work is a highly technical specialty, quite different in many respects from appraisals for the purpose of adjusting fire insurance losses, for mortgage purposes, or even for purposes of purchase or sale. In eminent domain cases the personal equation is not present, as it is in these other types of work. Here the appraiser is dealing more with technical rules of law, determined either by statutes or by long-established precedents, or both, and his testimony is scrutinized in a searching cross-examination by a specialist who may be presumed to know these technical rules of law and their application to the case at bar.

APPRAISER MUST UNDERSTAND LAW

For that reason, industry is the first qualification to be considered. The appraiser should have an understanding of these rules of law, and this can be acquired only by study. It is presumed, of course, that he knows valuations and is accustomed to consider all of the factors that influence or make up value. Unless he knows the application of the rules of law in eminent domain cases, he may find that the factors to which he gives most prominence are of little import; whereas factors which he may look upon lightly, or even may exclude from his consideration, are of the utmost significance and will receive the closest and most discriminating scrutiny by opposing counsel and by the court.

Many otherwise shrewd and intelligent appraisers appear in court woefully unprepared as witnesses because of their failure to appreciate the technical and special nature of the task that confronts them. Either their minds do not grasp the scope of eminent domain appraising, or they lack the industry to fit themselves for the job. It is not enough that a capable trial lawyer guide the appraiser in his direct testimony. Such a witness may give plausible and impressive evidence in his direct testimony, only to have it torn to shreds on cross-examination by a keen lawyer who quickly perceives whether the supposed expert really "knows his stuff," or whether he is superficial and uninformed as to the legal foundation of his case.

Mastery of these rules of law and of the controlling precedents in any jurisdiction is not easily achieved; but it is by no means beyond the grasp of an intelligent layman. An experienced lawyer can acquaint the appraiser with the legal principles involved and can cite to him the relatively small number of cases that explain these principles. A reasonable amount of study and a few questions should suffice to give the appraiser a workable foundation, upon which he may build according to his resourcefulness and intelligence. The trial lawyer must lean heavily upon his witness. The lawyer is neither a real estate expert nor an appraiser, and the witness should not expect the lawyer to know instinctively all of the considerations that make for value or lack of value. In these matters the witness should instruct the lawyer.

*Robert P. Butler is United States District Attorney for Connecticut. He is a trial attorney of many years' experience and as Corporation Counsel of the city of Hartford has conducted many eminent domain cases. He has represented numerous appellants in similar proceedings and frequently has served as committee of the Court (referee) in determining condemnation issues.

The witness must know, and be prepared to demonstrate, the relationship of the property in question to other properties within that area wherein an influence for good or bad may be asserted by other properties. He must know past trends and future probabilities (not possibilities), and he must be prepared to support his testimony and his judgment as to these factors by illustrations drawn from his own knowledge or experience or from the demonstrable experience of others. This calls for intelligence, for resourcefulness, for ingenuity, for discrimination — in short, for skill. A witness who has these qualities speaks with authority. He carries the conviction of truth, and to counsel he is more precious than much fine gold.

INTEGRITY AN ESSENTIAL QUALIFICATION OF APPRAISER

But these qualities of industry and intelligence are worth little unless they are buttressed by unquestioned integrity. Too often the appraiser is asked by the property owner, or by his counsel, to be prepared to substantiate a predetermined value. Such a situation should present no problem to the prospective witness. He should promptly decline the assignment. A great criminal trial lawyer once said to a jury: "We have presented no experts that can be bought by the dozens by both sides. In this case their testimony would be valueless."

Once a court gets the idea that an appraiser is trying to establish and maintain a predetermined valuation, instead of trying to discover and demonstrate a true valuation, the case is well on the way to being lost and the appraiser discredited.

If a case is so weak that the appraiser must resort to trickery or sham, or must give his testimony with his tongue in his cheek, he is no longer an appraiser but an advocate; he is a detriment to his client, a bad tool to the lawyer, and a disgrace to his profession.

If the question of a predetermined valuation is presented for consideration, the appraiser should make preliminary inquiries to ascertain whether that predetermined valuation is fair and honest, and whether it can be sustained by fair and honest testimony. If so, he may be justified in undertaking the task. If not, he can never justify his undertaking and had better drop the case. Appraisers will lose fat fees occasionally if they pursue such a course, but they will find in the long run that there is no satisfactory substitute for integrity. Without it no enduring reputation can be built, and without such reputation an appraiser's services are no longer in demand.

PRELIMINARY REPORTS IMPORTANT TO LAWYER

In addition to the general qualities outlined above, there are other attributes that a lawyer seeks in an appraiser. Clear and comprehensive preliminary reports are probably the first of these. If there should be (and there usually is) more than one approach to the question of value, each of these approaches should be treated as a separate problem and every detail clearly outlined for the benefit of the lawyer. Here, surely, the appraiser should assume that he is better informed and more capable than the lawyer, and he should be prepared to educate the lawyer just as he expects the lawyer to educate him in those matters which fall within the latter's field.

In the conference or conferences between the two, each should gain a complete understanding of the mind of the other. Before they go to court, the lawyer should master the fundamentals of value which his witness will present, and the witness should be master of the legal principles involved in the presentation.

The fundamentals of direct examination are contained in an article on "Court Testimony" by George L. Schmutz, M.A.I.,

printed in a recent issue of *The Journal of the American Institute of Real Estate Appraisers*,[1] wherein three questions are presented that cover generally the field of direct examination. They are:

1. When you received this appraisal assignment, what did you do?
2. What did you consider?
3. What were your conclusions?

This part of the testimony is relatively simple. It is on cross-examination that the witness shows his real colors. Many expert witnesses destroy or impair the value of their testimony because they cannot forget the fact that they are "experts." If they are not experts, they should not be there. If they are there, it should go without saying that they are experts, and the witness, above all, should take this for granted. It is most unwise for a witness to indulge in "wisecracks" or to be "smart" on the witness stand; and, above all, the witness should never fence with nor quarrel with the opposing counsel, for the latter invariably has the advantage. If counsel wishes to do battle with his opponent, that is his privilege. He is, or should be, the advocate — the witness, never.

Both on direct and cross-examination, the opinions of the witness (and his evidence is largely opinion) should be stated firmly, but with dignity and with courtesy. The witness must make sure that he understands every question before he replies to it, and if he is neither pugnacious nor flustered, his reply will carry much more weight.

By his calm and courteous attitude the witness not only will enhance the dignity of his calling, but will impress the court with the truth of his conviction. And that is what wins cases.

[1] *The Journal of the American Institute of Real Estate Appraisers*, Vol. V, No. 2 (Chicago: American Institute of Real Estate Appraisers, April, 1937), pp. 130-142.

The Appraisal Docket

Cases, decisions, and other matters involving rulings and precedents affecting real estate and valuation

William Wilson, Editor

John C. Butler, Assistant Editor

As gratifying as the Gallup Poll's assurance to the anxious politician is the elan with which a lawyer views the decision of the higher court sustaining his appeal. Vicariously we are permitted to share the gratification afforded by a recent case wherein our challenge to the logic of the lower court's decision was upheld. We for the moment have become oracular!

CONSTITUTIONAL CANTICLES

Prognostication Proved

We mentioned in a preceding issue[1] the case of *Central Savings Bank* v. *City of New York*, 5 N.Y.S. 451 (1938) which had held constitutional that provision of the New York Multiple Dwelling Law which permitted the city of New York to make repairs, in instances wherein the owners refused so to do, upon old law tenements and to place the cost thereof as a lien prior to existing mortgages and encumbrances. The court sought to justify its decision by remarking that the improvements bettered the security of the mortgage. We held this to be specious reasoning, pointing out that though the physical value of the property may be enhanced, the economic value, derived from its rent-producing capacity, would not likely be affected, so that in the real sense the mortgage lien would certainly be impaired.

The case was taken to the New York Court of Appeals wherein the decision was reversed and the pertinent provision of the Multiple Dwelling Law was held unconstitutional on the two grounds that the property of the mortgagee was taken without due process of law and that the contractual obligation was impaired. *Central Savings Bank* v. *City of New York*, 279 N.Y. 266, 18 N.E. 2d 151 (1938). The court in its opinion remarked:

> "It is no answer to this suggestion to say that the property has been improved to the extent of the expenditures. They may or may not add anything to the land value, and on foreclosure sale might not bring one penny more to the mortgagee. It is common knowledge that in New York city many buildings add nothing to the land value. The improvements may or may not enhance the value of the mortgagee's security. It is a speculation, with the chances greatly against their doing so. We may fairly assume that the lien given to the city for the required improvements very materially affects the mortgage security, the property of the mortgagee, and abrogates the contract which he has made with the mortgagor." (Page 155)

Prognostication Prescient

Emboldened by the New York case, we shall try our hand with a second situation—one which concerns the constitutionality of the New York law restricting the amount of the deficiency judgment in ac-

[1] "The Appraisal Docket," *The Journal of the American Institute of Real Estate Appraisers* (October, 1938, Vol. VI, No. 4), pp. 362-363.

tions in equity[2] or at law[3] upon mortgage indebtednesses to the excess of the indebtedness over the "fair and reasonable" market value of the property. (Formerly, the deficiency was established by the excess of the indebtedness over the amount of the bid at the foreclosure.[4]) In the case of *Honeyman* v. *Clark*, 278 N.Y. 467, 17 N.E. 2d 131 (1938), the plaintiff foreclosed on a mortgage given to secure a debt of $15,000. The plaintiff was the purchaser at the foreclosure sale and bid thereat the sum of $7,500, leaving a deficiency of $9,590. The lower court found that the value of the property was equal to the debt and denied the application for a deficiency judgment. The Court of Appeals, relying upon its former decisions[5] (an interesting facet of which was the remark[6] of the court that the law was but temporary[7]), sustained the constitutionality of the legislation as against the contention that it was in impairment of contractual obligations.[8] An appeal was

[2]"No judgment shall be granted for any residue of the debt remaining unsatisfied as prescribed by the preceding section where an action to foreclose the mortgage has been or shall be commenced during the emergency or where the mortgaged property shall be sold during the emergency, except as herein provided. Simultaneously with the making of a motion for an order confirming the sale provided such motion is made within ninety days after the date of the consummation of the sale by the delivery of the proper deed of conveyance to the purchaser in all cases where the sale is held after the date this section as hereby amended takes effect and in all cases where the sale was held prior to the date this section as hereby amended takes effect and said sale has not heretofore been confirmed, then within ninety days from the date this section as hereby amended takes effect or within ninety days after the date of the consummation of the sale by delivery of the proper deed of conveyance to the purchaser, regardless of whether the sale prior or subsequent to or on the date this section as hereby amended takes effect, the party to whom such residue shall be owing may make a motion in the action for leave to enter a deficiency judgment upon notice to the party against whom such judgment is sought or the attorney who shall have appeared for such party in such action. Such notice shall be served personally or in such other manner as the court may direct. Upon such motion the court, whether or not the respondent appears, shall determine, upon affidavit or otherwise as it shall direct, the fair and reasonable market value of the mortgaged premises as of the date such premises were bid in at auction or such nearest earlier date as there shall have been any market value thereof and shall make an order directing the entry of a deficiency judgment. Such deficiency judgment shall be for an amount equal to the sum of the amount owing by the party liable as determined by the judgment with interest, plus the amount owing on all prior liens and encumbrances with interest, plus costs and disbursements of the action including the referee's fee and disbursements, less the market value as determined by the court or the sale price of the property whichever shall be higher. If no motion for a deficiency judgment shall be made as herein prescribed the proceeds of the sale regardless of amount shall be deemed to be in full satisfaction of the mortgage debt and no right to recover any deficiency in any action or proceeding shall exist.

"Notwithstanding the foregoing provisions and irrespective of whether a motion for a deficiency judgment shall have been made or, if made, shall have been denied, the court shall direct that all moneys remaining in the hands of a receiver of the rents and profits appointed in the action, after the payment of the receiver's fees and the expenses of the receivership, or any moneys remaining in the hands of a mortgagee in possession or an assignee of the rents and profits of said premises, shall be paid to the plaintiff to the extent of the amount, if any, by which the judgment of foreclosure and sale exceeds the amount paid for said property upon said sale." New York Civil Practice Act, § 1083-a.

[3]"In any action pending at the time this section as hereby added takes effect, or hereafter commenced during the emergency, other than an action to foreclose a mortgage, to recover a judgment for any indebtedness secured by a mortgage on real property and which originated simultaneously with such mortgage and which is secured solely by such mortgage, against any person or corporation directly or indirectly or contingently liable therefor, any party against whom a money judgment is demanded, shall be entitled to set off the fair and reasonable market value of the mortgaged property less the amounts owing on prior liens and encumbrances. In any action to foreclose the mortgage commenced after the emergency as defined by the law shall have expired, a deficiency judgment may be recovered as though this section had not been enacted but the amount of any money judgment recovered as provided in this section shall be deducted in computing such deficiency judgment." New York Civil Practice Act, § 1083-b.

[4]*Heiman* v. *Bishop*, 272 N.Y. 83, 4 N.E. 2d 944 (1936).

[5]*Klinke* v. *Samuels*, 264 N.Y. 144, 190 N.E. 324 (1934); *City Bank Farmers' Trust Co.* v. *Ardlea Corporation*, 267 N.Y. 224, 196 N.E. 34 (1935); and *Honeyman* v. *Hanan*, 275 N.Y. 382, 9 N.E. 2d 970 (1937). This last case has certainly run the gamut. The peregrinations to and fro Gog and Magog have (not counting the decisions of the intermediate court) been as follows:

Honeyman v. *Hanan*, 271 N.E. 564, 3 N.E. 2d 186 (1936) —*per curiam*: judgment of the Supreme Court of New York, Appellate Division, affirming a judgment of the Special Term dismissing the complaint, affirmed.

Honeyman v. *Hanan*, 271 N.Y. 662, 3 N.E. 2d 473 (1936) —motion to amend remittitur (so as to reflect the constitutional aspect of the case) granted.

Honeyman v. *Hanan*, 300 U.S. 14 (1937)—judgment in 3 N.E. 2d 473 vacated so as to present the precise nature of the Federal question.

Honeyman v. *Hanan*, 275 N.Y. 382, 9 N.E. 2d 970 (1937) —decision upholding constitutionality of §§ 1083-a and 1083-b.

Honeyman v. *Hanan*, 302 U.S. 375 (1937)—appeal dismissed, no substantial Federal question being raised.

Honeyman v. *Hanan*, 274 N.Y. 490, 8 N.E. 2d 618 (1937) —motion to amend remittitur set down for May 17, 1937.

Honeyman v. *Hanan*, 275 N.Y. 625, 11 N.E. 2d 788 (1937)—motion to amend remittitur granted.

[6]In *Klinke* v. *Samuels*, 264 N.Y. 144, 190 N.E. 324 (1934), it was said concerning §§ 1083-a and 1083-b (which laws were enacted August 26, 1933):

"As to the constitutionality of these provisions we must remember that the limitation upon the remedy in both or all instances is until July 1, 1934. There being no market for real estate of any kind, and the banks refusing to loan money on the best of real estate security, owners were caught, as it were, in a trap due to conditions over which no one had control and for which no relief was at hand. Value was in the property, but the value could not be obtained nor anything like it. To prevent worse and more extensive evils and suffering, the Legislature had asked, through these laws, for security holders to wait a reasonable time for universal economic conditions to improve, provided interest and taxes are paid.

"*After next July, all remedies, so far as the present laws apply, will again be open to the mortgage creditors.*" (Italics, ours.) (Page 326)

[7]The amendment of 1934 (April 23) extended the period of "emergency" to July 1, 1935.

The amendment of 1935 (January 18) extended the period of "emergency" to July 1, 1936.

The amendment of 1936 (March 6) extended the period of "emergency" to July 1, 1937.

The amendment of 1937 (March 18) extended the period of "emergency" to July 1, 1938.

The amendment of 1938 (April 6) extended the period of "emergency" to July 1, 1939.

[8]Constitution of the United States, Article 1, § 10, "No state shall . . . . pass any . . . . law impairing the obligation of contract . . . ."

docketed with the Supreme Court of the United States, and the case there submitted on February 10, 1939.

The Supreme Court of the United States has promulgated the suave theory that contractual obligations are not constitutionally impaired by a law which modifies the remedy for the enforcement of the contract but which does not impair the substantial rights secured by it. *Home Building and Loan Association* v. *Blaisdell*, 290 U.S. 398 (1934).[9] What purports to be a positive constitutional limitation has thus been metamorphosed into a relative limitation. The dangerous extent in logic of this theory is well illustrated by the fact that statutes of limitation are sometimes held in bar of the enforcement, though not of the right. *Campbell* v. *Holt*, 115 U.S. 620 (1885). The theory finds better justification in the contemporary field of humanitarianism than in the domain of logic. For what is a right without a remedy? It is to be reluctantly averred that the court now has forged a two-edged blade, which it is free to swing either this way or that, whose cut swathe increases our constitutional penumbrae.

Were it not for the fact that the New York legislation under consideration has been extended five times, each on the continuing plea of "emergency," we would feel constrained, upon the basis of the Blaisdell Case, to predict its constitutionality. However, the tinsel brightness of repetitious emergencies becomes tarnished with too much use. Their diminuendo is a matter judicially noticed. *Chastleton Corporation* v. *Sinclair*, 264 U.S. 267 U.S. 543 (1923).[10] An emergency, it is said, does not create constitutional powers, but authorizes their use.[11] The justification of the emergency power (and the consequent abrogation of the constitutional limitation) fails, however, when the emergency becomes the ordinary.[12]

Our prediction (and sad we are that we cannot make it as Delphic as a constitutional canticle) is that if the Supreme Court of the United States once is convinced (or resigned to the fact) that a Federal question is presented in the Honeyman v. Clark Case,[13] it will by a divided court strike down the New York legislation on the doctrine of the Chastleton Case.

We are strengthened in our conclusion by the holding of the recent case of *Home Owners' Loan Corporation* v. *Margolis*, 6

[9]The constitutional challenge to the contract clause of the Federal constitution there under consideration was presented by the Minnesota moratorium statute, passed April 18, 1933, which extended the period of redemption from foreclosure sales to May 1, 1935. The statute was held constitutional.

[10]This case concerned an extension of the famous World War rent legislation of the District of Columbia, whereby on the plea of demand greatly exceeding supply, rents of real property were regulated in the public interest. The original act was passed on October 22, 1919, and was limited to expire in two years. Its constitutionality had been upheld. *Block* v. *Hirsh*, 265 U.S. 135 (1921). The act was subsequently continued in force as a subsequent act until May 22, 1922, when a third act, declaring the emergency still existed, continued the law until May 22, 1924. The validity of the extension was questioned (*Chastleton Corporation* v. *Sinclair*, 264 U.S. 267 U.S. 543), Justice Holmes saying:

> "A law depending upon the existence of an emergency or other state of facts to uphold it may cease to operate if the emergency ceases or the facts change even though valid when passed." (Pages 547-548)

[11]Mr. Chief Justice Hughes, in the Blaisdell Case (290 U.S. 398):

> "Emergency does not create power. Emergency does not increase granted power or remove or diminish the restrictions imposed upon power granted or reserved. . . . .
> "While emergency does not create power, emergency may furnish the occasion for the exercise of the power. . . . ." (Pages 425-426)

[12]The Nebraska mortgage moratorium act was held unconstitutional in *First Trust Co. of Lincoln* v. *Smith*, 134 Neb. 84, 277 N.W. 762 (1938). The act there had been several times extended. The Court, anent the "emergency," pithily said:

> "It appears that there is no crisis now prevailing which involves a general paralysis of business and finance, and that the unfortunate condition now confronting us is strictly a 'continued depression.'" (Page 770)

Similarly a very recent case handed down by the Supreme Court of Iowa held the statutory extension of the mortgage moratorium law in that state to be unconstitutional. *First Trust Joint Stock Land Bank of Chicago* v. *Arp.*——*Ia.*——, 283 N.W. 441 (1939). The moratorium legislation was first enacted in Iowa on February 9, 1933. It was extended on February 8, 1935, and re-extended on February 19, 1937, to March 1, 1939. The court said at page 443:

> "Emergency in order to justify the intervention of the reserve police power must be temporary or it cannot be said to be an emergency. If a so-called emergency exists beyond a temporary period then it is no longer an emergency but a status and can furnish no basis or authority for legislative action in contravention of or inconsistent with the provisions of the State and Federal constitutions. The existence of an emergency is necessarily a fact question. While declaration of the executive and pronouncements of the Legislature are entitled to great weight and should be carefully considered, yet, the fact question still exists, and this can be determined by record facts, history of current events, and common knowledge and information. In other words, a court, in determining the existence of an emergency, may and should take judicial notice of conditions existing at the time the emergency or its continued existence is questioned." (Page 443)

[13]See footnote 5, *supra*.

N.Y. Supp. 2d. 432 (1938). That case held that the 1938 amendment to § 1083 of the New York Civil Practice Act was unconstitutional as to those mortgages made prior to such amendment. The amendment, which was not prefaced by or pleaded as a temporary emergency, but was designed as a permanent rule, purported to limit deficiency judgments to the difference between the indebtedness less the market value of the property or its sale price, whichever shall be the higher.[14]

Interesting in this connection is the case of *In re Board of Water Supply of City of New York*, 277 N.Y. 452, 14 N.E. 2d 789 (1938). Such was a condemnation proceeding, where value was to be established as of November 16, 1936. The Court sanctioned the admission of testimony as to the market value of the property in question as of October, 1930, when it was claimed the property last had a market value. Precedent was found in the legislative declaration of policy contained in § 1083-a,[15] which provides that where there is no market at the date when value is to be determined, value is then to be fixed "at such nearest earlier date as there shall have been any market value thereof." Why not say, baldly but at least honestly, that value is not to be ascertained by reference to the present market, but by reference to the market as the courts and the legislature dream it should be!

[14]The court said in rendering its decision:

"The view was entertained that when the right to a deficiency judgment exists at the time when a mortgage is executed, it is a part of the contract which may not be impaired by subsequent legislation. *New York Life Insurance Co.* v. *H. & J. Guttag Corporation*, 265 N.Y. 292, 296, 192 N.E. 481. Even though emergencies may awake legislative powers that sleep in normal times, no emergency is asserted by chapter 510 of the Laws of 1938. The Court of Appeals has gone no further than to hold such legislation constitutional when reasonably seeking only temporary relief. *Klinke* v. *Samuels*, 264 N.Y. 144, 149, 190 N.E. 324. Chapter 510 of the Laws of 1938 is not designed for temporary relief, but as the future policy of the State toward deficiency judgments for all time. It, therefore, seemed to follow that section 1083, as amended by chapter 510 of the Laws of 1938, could not constitutionally apply to the mortgage which was executed as this one was before that Act took effect and that to hold otherwise would render chapter 510 of the Laws of 1938 unconstitutional." (Page 433)

[15]See footnote 2, *supra*.

PATERNALISM
or
THE CALIFORNIA REAL ESTATE ACT

RESIGNEDLY we accept the inexorable enroachment of paternalistic legislation. Such phenomena have become increasingly evident on all sides and find tolerance with the courts as the inevitable concomitant of the growing complexity and integration of society. We are still imbued, however, with such a Rip Van Winklian humor as to smack our chops and rub our hands over the dying embers of *caveat emptor* (Let the buyer beware!), so that our reflex mortis has not yet ceased. We become momentarily convulsive, for example, in our contemplation of the recent (1935) addition to the California Real Estate Act designed to protect the purchaser of a subdivision lot from the possible fraud, deceit, and misrepresentation of the subdivider. Such legislation (the court's paraphrase of which is quoted below[16]) has been held constitutionally valid as a proper exercise of the state's police power, as against the contention that it imposes unreasonable burdens on the exer-

[16]Section 20a of the act provides that prior to the time when subdivided lands are offered for sale or lease, the owner, his agent, or subdivider shall notify the real estate commissioner in writing of his intention to sell, and in such notice shall give the name and address of the owner and the subdivider; description and area of the land; true statement of the condition of the title, particularly including all encumbrances; the terms or conditions on which it is intended to dispose of the land; and copies of contracts intended to be used. The commissioner may require "such additional information concerning the project as he may deem necessary," and may prepare a questionnaire to be answered. Section 20b authorizes the commissioner, at the expense of the owner, his agent, or subdivider, to investigate any subdivision offered for sale or lease and make public his findings. Section 20e provides that the commissioner may issue an order prohibiting the sale or lease of the property if his examination shows that the sale or lease "would constitute misrepresentation to or deceit or fraud of the purchasers of lots or parcels in such subdivision." This examination is followed by a public report (Sec. 20e), and before any prohibitory order, a hearing must be held (Sec. 20f). After the project has been submitted to the real estate divisions, no material changes may be made without first notifying the division (Sec. 20g). If the land is subject to a lien or encumbrance, provision must be made enabling the vendor to deliver title to each parcel sold free of such lien or encumbrance, upon completion of performance by the purchaser. Sec. 20h. For the purpose of the act, "subdivision" is defined as "land or lands divided or proposed to be divided for the purpose of sale or lease, whether immediate or future, into five or more lots or parcels." Sec. 20j. Violation of these sections is made punishable by imprisonment in the county jail for not exceeding two years, or a fine not exceeding $2,000, and by suspension or revocation of a real estate broker's license. Sec. 20 1.

cise of property rights. *In re Sidebotham*, —— Cal. ——, 85 P. 2d 453 (1938). The ratiocination of the Court proceeded as follows:

> "The assertion that this is not valid police power legislation because it benefits only a special class, the purchasers and lessees of subdivided real estate, and not the whole public is without substance. The police power may be, and usually is, exercised for the purpose of protecting particular classes of the public in need of such protection, and it is rare indeed that a single law includes everyone in the scope of its regulations. The object of the present law, prevention of fraud and sharp practices in a type of real estate transaction peculiarly open to such abuses, is obviously legitimate; and the method involving investigation and disclosure of certain essential facts, and a protection for the innocent purchaser against loss of his land by foreclosure of the underlying mortgage, is perfectly reasonable. A safeguard against arbitrary action is provided in the requirement of a public report of the commissioner's investigation and a public hearing on any contemplated prohibitory order." (Page 454)

We are thus presented with the anomaly that one not only has the constitutional right to be a fool, but that constitutionally one may demand protection from the consequences of what one has a right to be and do. Sitting, as we do all day long, in our "well-stocked clubs" (for where else would we be with such ideas?) we become Alices in Wonderland and mumble to ourselves the adage that angels rush in where fools fear to tread.

AND AGAIN, PATERNALISM

FOR the benefit of those who would add to their reference notes, we shall without comment mention that housing authority acts have been given the constitutional accolade in six more states other than the seven which we mentioned in a preceding issue. The list has therefore grown to thirteen, which are named below.[17] Interesting it is to know that such acts have been passed in thirty-three states.[18]

[17] 1. ALABAMA—*In re Opinion of Justices*, 235 Ala. 493, 179 So. 535 (1938).
2. FLORIDA—*Marvin* v. *Housing Authority of Jacksonville*,——Fla.——, 183 So. 145 (1938).
3. GEORGIA—*Williamson* v. *Housing Authority*, 186 Ga. 673, 199 S.E. 43 (1938).
4. ILLINOIS—*Krause* v. *Peoria Housing Authority*, 370 Ill. 356, 19 N.E. 2d 193 (1939).
5. INDIANA—*Edward* v. *Housing Authority of City of Muncie*,——Ind.——, 19 N.E. 2d 771 (1939).
6. KENTUCKY—*Spahn* v. *Stewart*, 268 Ky. 97, 103 S.W. 2d 651 (1937).
7. LOUISIANA—*State* v. *Housing Authority of New Orleans*, 190 La. 710, 182 La. 725 (1938).
8. MONTANA—*Rutherford* v. *City of Great Falls*,—— Mont.——, 86 Pac. 2d 656 (1939).
9. NEW YORK—*New York City Housing Authority* v. *Muller*, 270 N.Y. 333, 1 N.E. 2d 153, 105 A.L.R. 905 (1936).
10. NORTH CAROLINA—*Wells* v. *Housing Authority of City of Wilmington*, 213 N.C. 744, 197 S.E. 693 (1938).
11. PENNSYLVANIA—*Dornan* v. *Philadelphia Housing Authority*, 331 Pa. 209, 200 A. 834 (1938).
12. SOUTH CAROLINA—*McNulty* v. *Owens*, 188 S.C. 377, 199 S.E. 425 (1938).
13. TENNESSEE—*Knoxville Housing Authority* v. *City of Knoxville*,——Tenn.——, 123 S.W. 2d 1085 (1939).

[18] *Housing Legal Digest*, No. 55 (February, 1939). The states therein listed which do not have such legislation are as follows: Arizona, Idaho, Iowa, Kansas, Maine, Minnesota, Missouri, Nevada, New Hampshire, New Mexico, Oklahoma, South Dakota, Utah, Washington, and Wyoming.

TAX LITIGATION

WE are indebted to the indefatigable Mr. Hyder for giving us the scent of two decisions which he considers should be of significant interest to Institute members. We pause briefly to remark again of our appreciation for contributions of this nature and to exhort our readers to send us references to legal decisions which they would like to see placed in these columns.

In re Estate Taxes

Weber v. *Rasquin*, 101 F 2d. 62 (C.C.A. 2nd, 1939) concerned the action by the executrix of the estate of John W. Weber to recover the amount of estate taxes claimed to have been illegally exacted. The tax was assessed against the devolution of 1,497 shares of stock of William Ulmer, Inc., a New York corporation whose total capital issue (5,500 shares of $100 par value stock) was closely held. The corporation, prior to 1919, had been engaged in the manufacture and sale of malt beverages, but with the advent of prohibition ceased such activity and concerned itself with the liquidation of its

assets which consisted chiefly of real property and mortgages thereof. The Commissioner of Internal Revenue appraised the property by a method which made no allowance for the difficulty in liquidating the assets. The Circuit Court of Appeals held this to be error and supported its finding of a lower (or liquidated) value by comparison with a figure computed by the capitalization at 6 per cent of the average annual earnings of the properties for the immediately preceding five-year period (1928-1932):

> "The amount of $26,592.25, computed as the average yearly earnings, would if capitalized at 6% show a principal of less than $500,000. [Editors' note: The Commissioner found the net worth of the corporation to be $1,007,470.44.] While we do not say that a rate of 6% would necessarily be proper for estimating the return upon the real estate and mortgages, the fact that a capitalization on that basis would indicate a value of less than half that found by the appraisers tends to show that the net worth which they reported should not have been adopted as the sole basis for determining the value of the decedent's stock."
>
> The trial judge "disregarded the Treasury Regulations, and instead of determining a value for the stock of decedent by taking into account (1) his fractional share of the net worth of the corporation; (2) the expense of liquidation of the assets; and (3) the earning power and dividend-paying capacity of the stock, he reached a conclusion based upon a consideration only of the net worth." (Page 64)

Lessee's Improvements as Income to Lessor

The case of *M. E. Blatt Co.* v. *United States*, 305 U.S. 267 (1938) concerned the propriety of the Commissioner's addition to the lessor's income (fiscal year ending January 31, 1932) of one tenth the cost (depreciated to the end of the ten-year lease term) of improvements made by a lessee to a building so as to adapt it for use as a motion-picture theatre, the improvements to become the property of the lessor upon the termination of the leasehold. The Supreme Court of the United States held that the one-tenth portion of the depreciated cost of the improvements was not subject to income tax either on the ground that it was rent or taxable income other than rent. The Court further declared that the value of property is not susceptible to addition of the cost of its constituent items[19] and that the enhancement in value caused by the improvements is not realized income of the lessor.[20]

THE ALAS AND ALACK OF TWO INVESTMENTS IN REAL ESTATE ASSETS

INTERESTING from a factual point of view is the recent case of *Linch* v. *Heuck*, 58 Ohio App. 406, 16 N.E. 2d 613 (1938), which concerned itself with the valuation of a property whose extrinsic value to its purchaser was concededly in excess of its market value. The Court held that the valuation for tax purposes of the property was suitably under the circumstances to be left to the discretion of Board of Revision and Tax Commission of Ohio. The circumstances are aptly set forth by the Court in its opinion:

> "The plaintiff, in order to satisfy certain peculiar requirements of his family, determined upon the purchase of the particular real property involved herein. It was then unimproved. The then owner of the property, it is apparent, was just as determined that he should not acquire the property. The plaintiff, however, made an offer at such a price that the then owner concluded to accept the condition, admittedly more than twice the

[19] "But present or future value, however ascertained, is single in substance; it cannot be arrived at by mere summation of actual or estimated cost of constituent elements, new or depreciated." (Page 279)

[20] "But, assuming that at some time value of the improvements would be income of lessor, it cannot be reasonably assigned to the year in which they were installed. The commissioner found that at the end of the term some would be worthless and excluded them. He also excluded depreciation of other items. There exclusions imply that elements which will not outlast lessee's right to use are not at any time income of lessor. The inclusion of the remaining value is to hold that petitioner's right to have them as a part of the building at expiration of lease constitutes income in the first year of the term in an amount equal to their estimated value at the end of the term without any deduction to obtain present worth as of date of installation. It may be assumed that, subject to the lease, lessor became owner of the improvements at the time they were made. But it had no right to use or dispose of them during the term. Mere acquisition of that sort did not amount to contemporaneous realization of gain within the meaning of the statute." (Page 280)

market value of the unimproved real estate. Even at the exorbitant price paid, the seller was able, in view of the situation, to impose upon the plaintiff purchaser restrictions upon the use of the premises which greatly hampered the convenient adaptation thereof for residence purposes, and greatly increased the amount of money required to develop the property for a residence suitable to the use of plaintiff. The net result of these circumstances was to cause the plaintiff to spend approximately $180,000 for a lot and residence which competent realtors estimate was not saleable for more than the amount found to be a fair tax value by the trial court, to wit, $50,000.

"The county auditor in 1931 made a county-wide appraisal of real property. He concluded that the ordinary mechanical index system employed in the valuation of ordinary residences was inappropriate to residences of the type considered here. As to these, he adopted a cubic content standard, each such residence being actually measured. He then employed experts from whom he secured opinions as to the reproduction cost per cubic foot of such buildings. In addition to an ordinary obsolescence reduction, the auditor also applied a devaluation of 21% based upon bad judgment in the expenditure of money in construction and location. His conclusion was, as before stated, that, taking all of these factors into consideration, the value in money of the residence and property was $94,600, approximately one-half of the admitted cost of the property and structure.

"The Tax Commission, upon appeal, reduced this amount to $76,340, but upon what basis does not appear." (Pages 613-614)

Interesting also from a trust point of view is the recent case of *Feist* v. *Fifth Avenue Bank of New York*, 5 N.Y.S. 736 (1938), which concerned the construction of an agreement of trust which created a life estate for the benefit of the settlor's invalid son, with remainders over. The trustee was authorized to invest the funds only in "bonds of the United States. State of New York, City of New York, or guaranteed mortgages on improved real estate in the City of New York." The trustee (the named defendant bank) invested on June 3, 1931, $60,000 of the trust funds in a first mortgage of $90,000 covering certain premises at 319-323 East 45th Street, New York City. The premises were "improved" by three buildings (erected prior to 1932) of the type known as cold-water flats. The rents ranged from $20 to $25 a month for each apartment of six rooms. The net income of the buildings from February, 1931, to June, 1932, was at the rate of $1,400 per annum, after payment of taxes and operating expense but before payment of the annual interest charge of $5,400. In September, 1937, the trustee (which had acquired the property by foreclosure) directed the demolition of the buildings since it felt that with the decline in rentals it would be imprudent to invest the additional sums in the property in order to comply with the provisions of the recently enacted Multiple Dwelling Law. The property since had been used as a parking lot. The life beneficiary, whose income had ceased from the $60,000, brought suit, together with the remaindermen, to surcharge the trustee with that sum. The Court held that from a practical standpoint the property was not improved; that since the purpose of the trust was to provide income for the settlor's invalid son during the latter's life, the settlor had in mind that investments were to be made in real property *adequately* improved. The trustee was consequently surcharged the sum of $60,000.

The decision is, we submit, correct, though we hesitate to approve the Court's malassimilation of the word "improved." Better would it have been to say that the trust agreement limited the field of investment but still did not excuse the exercise of prudence in that field.

What to Read

Comments on recent surveys, books, and articles of interest to real estate appraisers

C. M. Jones, Editor — Librarian, American Institute of Real Estate Appraisers

BOOK REVIEWS

MONTHLY PAYMENT DIRECT REDUCTION LOAN AMORTIZATION SCHEDULES. *Boston, Massachusetts: Financial Publishing Company, 1938. 447 pp., $4.00.*

THIS excellent reference book should be on the desk of every appraiser, institution loan officer, real estate broker, and private lender. Attorneys handling estate funds and trust officers also will find it very useful.

While the idea of self-liquidating mortgages bearing constant, equal monthly payments is not new, in the past it usually has been limited to the building and loan type of mortgage with a maturity of about eleven years. During recent years modern versions of this type of financing, with maturities up to twenty years and in amounts up to 90 per cent of the appraised value, have been publicized extensively by the Federal Housing Administration and now are widely used in various modified forms by lenders all over the United States.

A book of tables dealing with this type of mortgage financing has not to my knowledge been available previously to the general public.

The main tables of this book contain full schedules showing the working out of a loan of $1,000. Arrangement is by rates, starting with 4 per cent and progressing up to 8 per cent. Rates are shown for each ½ per cent, but special sections have been inserted for the rates of 5.4 per cent, 6.6 per cent, and 7.2 per cent, often used by building and loan associations. A special table for nineteen and one half years has also been inserted because of the large number of early F.H.A. loans written for that term. Each table assumes that the loan is to run for a definite period of years, and the payment shown is the one which will amortize the loan in this period.

For each rate there is a table showing the monthly payment per $1,000 for every year from one to twenty-five. The payment is divided into interest and principal due each month and the balance of the loan shown.

For example, at 5½ per cent, running for twenty years, the monthly payment per $1,000 is $6.88 (exact figure $6.878873).

In the table each of the 240 payments is shown as follows:

Time		Payment on		Balance of
Years	Months	Interest	Principal	Loan
1	0	$4.46	$2.42	$971.73
11	0	2.70	4.18	584.70
20	0	.03	6.20	0.00
			Final Payment	6.23

Following the twenty-five-year schedule of each rate is a series of three tables

showing fixed monthly payments of $7.00, $8.00, $9.00, and $10.00 per thousand and the working out of the loan based upon these payments.

A further set of tables printed on yellow paper shows the equal monthly payment necessary to amortize a loan of $1,000 over a term of any number of months from one month to twenty-eight years at rates from 3 per cent to 6 per cent by ¼ per cent and from 6½ per cent to 8 per cent by ½ per cent, also 5.4 per cent, 6.6 per cent, and 7.2 per cent.

The final set of tables shows interest for one month on all amounts up to $1,000 and on even thousands.

The size of the book is six and one fourth by nine and one fourth inches, with flexible cloth binding, printed on lightweight paper to reduce the thickness to about one inch.

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Macaulay, Frederick R. BOND YIELDS, INTEREST RATES, AND STOCK PRICES. *New York: National Bureau of Economic Research, Inc., 1938. 240 pp. + 351 pp. of tables and charts, $5.00.*

THIS volume is a general study of the subject to which the title alludes. It traces price and interest movements in the United States back to 1856.

One topic which Dr. Macaulay treats is the relation between short- and long-term bond yields. Furthermore, he questions the theory of most classical economists that there is a persistent similarity between the movements of bond yields and the movement of commodity prices. His chapters on the "Concept of Long Term Interest Rates" and "Interest Rates and Commodity Prices" are of particular interest to the appraising fraternity at large.

This work is not elementary, and it presupposes an elementary knowledge of the subject from both a theoretical and a statistical point of view.

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Williams, John Burr. THE THEORY OF INVESTMENT VALUE. *Cambridge, Massachusetts: Harvard University Press, 1938. 613 pp., $5.00.*

MR. WILLIAMS has written a volume which is both practical and theoretical in its aspects. Chapters which are most interesting are those on "Speculation and Investment," "The Rule of Present Worth," "The Future of Interest Rates," and "Where the Interest Rate is Determined."

The last half of the book gives specific case studies in valuation—via the method of capitalization — of General Motors, United States Steel, American Telephone and Telegraph, and several other stocks.

A knowledge of mathematics, while helpful to the reader, is not absolutely necessary. In short, the author has endeavored to relate abstract principles of economics to the practical problems of investment.

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NEW ARTICLES

"WHAT SUBWAYS WILL MEAN TO CHICAGO" by Charles E. Deleuw

Chicago's Consulting Engineer on Transportation Problems outlines in an interesting fashion plan details of the subway now under construction and tells how the completed project will benefit the city's transportation system. Endeavoring to cover this vast subject in a single article, he has formulated questions, with answers, which give an adequate understanding — "What Is the Initial System of Subways?" "How Will the Subways Be Built?" "How Will Initial Subways Be Used?" "How About Utility Structures?" "What Will Be the Immediate Benefits?" "Can the Loop Structure Be Removed?" "What Additional Subways Are in Prospect?" and "Are Two-Track Subways Adequate?" *The Economist, March 11, 1939, p. 5.*

●

"THE ECONOMIC LOCATION OF INDUSTRIAL PLANTS" by Herbert S. Swan

This is the first of two articles dealing with the community's problem in attracting new industries — an intensive study and application of the basic economic laws affecting the location and growth of different industries. The author contends that "factual data relating to the economic advantages possessed by different communities in the way of raw materials, labor, markets, transportation, fuel, and power will count as never before in the movements made by industry." *National Real Estate Journal, March, 1939, p. 18.*

●

"NON-CONFORMING USES DESTROY THE NEIGHBORHOOD" by Harland Bartholomew

The problem of "non-conforming uses" in our older neighborhoods is causing prospective home owners to seek newly developing suburban areas. The older the neighborhood, the higher the percentage of non-conforming uses. Our failure to protect neighborhoods properly has caused untold waste. Mr. Bartholomew suggests one way to reclaim these older residential sections in our cities. *The Journal of Land & Public Utility Economics, February, 1939, p. 96.*

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"REAL VALUES IN HOME OWNERSHIP" by Albert W. Atwood

"Shall I buy a house or a bond?" is a question frequently asked by the investor. This article is an attempt to give him the pros and cons of each. Mr. Atwood points out that the question is not whether securities or home ownership has the greater investment value—that the two forms of investment are not alternatives, but supplements or complements. "Home ownership," he says, "leads to security ownership, and many a security investor would never have become such if he had not first bought a house. One type of investment whets the appetite for the other." *Insured Mortgage Portfolio, March, 1939, p. 8.*

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"BLIGHT SEEN AS FOREMOST URBAN PROBLEM"

Louis H. Pink, the Chairman of the State Board of Housing, New York, in his report to Governor Lehman, points to blight as the most serious problem facing the state today. Little is being done to protect and preserve old neighborhoods. Instead everything is being done to improve transportation to take people out of

the cities into the suburbs. Mr. Pink believes that the problem of blight can be approached successfully only by a comprehensive program of subsidized public housing, limited-dividend housing, intelligent and socially useful large-scale production of housing by purely private enterprise, and wise investment of funds by financial institutions. *Real Estate Record, March 18, 1939, p. 7.*

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"LIFE INSURANCE COMPANY INVESTMENTS"

An annual study of current trends of life insurance company investment policies reveals an increase in the placement of funds in real estate mortgages. There has been a rapid rise in the economic importance of life insurance companies during the last third of a century. Their assets have been consistently upward. Today these companies hold 14 per cent of the total of all urban mortgages. Included in this article is a comprehensive analysis of life insurance company investments with tables, charts, graphs, and other statistical information. *Federal Home Loan Bank Review, March, 1939, p. 170.*

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"VALUATION OF REAL PROPERTY FOR TAXATION" by Alex M. Hamburg

This is a lawyer's viewpoint of the valuation of real estate for tax purposes. The article is written from the legal angle and is freely sprinkled with citations from court decisions. Here is the editor's resumé: "The principles governing the valuation of property must be taken out of the realm of conjecture and speculation. This does not necessarily mean the codification of precise formulae, or the fixation of rules of evidence. There is much to be said in favor of the establishment of principles having authority, certainty, and predicability. The present process of valuation must be brought in touch with reality; existing determinants of value must be made to serve as reliable guides." *Taxes, March 1939, p. 139.*

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"WHEN APPRAISING CONSIDER THE PRICE LEVEL" by Frank M. Stanley

"The importance of current price level and its application to appraisal of real estate must not be overlooked by the appraiser, particularly where he is trying to project the value of real estate into the future." During time of inflation, such as the author believes we are going through now, the appraiser should take note of price level trends particularly and lean toward conservative appraisals. He then can protect his valuation through a considerable part of the period of decrease in price level. *Real Estate, April 1, 1939, p. 12.*

●

"THE VALUATION OF HILLSIDE PROPERTIES" by Belden Morgan

The author presents the results of a lively discussion by a number of appraisers in Los Angeles, a section which has level as well as hillside property. In logical order, the advantages and disadvantages of hillside property are listed, with the conclusion that the disadvantages outweigh the advantages. The purpose of the discussion is to give appraisers a better understanding of market reaction to this type of property. *The Review of the Society of Residential Appraisers, March, 1939, p. 12.*

NEW M. A. I.s

ROBERT S. HAY, STAMFORD, CONN.

Born, East Orange, New Jersey, October, 1900; Past President and Past Secretary, Stamford Real Estate Board, Inc.; professional territory extends from East Portchester to Westport, Connecticut; graduate, Wharton School of Finance & Commerce, University of Pennsylvania; member, State and National Committees on Real Estate Taxation, 1934; member, Advisory Committee, Stamford Federal Housing Committee, 1935; supervised real property inventory of Stamford, 1934; nine years' experience as a real estate broker; eight years' experience in appraising real estate, including the valuation of acreage, residences, gas stations, business properties, resort properties, apartment houses, and water-front property; qualified in court as an expert on the value of residential and business properties.

EARL DONALD KEEFER, MIAMI BEACH, FLA.

Born, Alvo, Nebraska, December, 1890; proprietor of a general real estate office; President, Miami Beach Realty Board; Chairman, Standing Appraisal Committee, Miami Beach Realty Board; professional territory covers southeast Florida; three years at University of California; six years in Europe, the last four years as a member of the Unofficial American Delegation to the Reparation Commission; completed Case-Study Courses, Real Estate Appraisal I, II, and III, conducted by the American Institute of Real Estate Appraisers at The University of Chicago, 1936; liquidator of the Miami Beach Bank & Trust Company, 1930-32; licensed real estate broker in the state of Florida; nine years' experience in real estate appraising, including the valuation of single-family homes, apartments, hotels, office buildings, and commercial properties; qualified in court as an expert on the value of real property.

WARD FARNSWORTH, CHICAGO, ILL.

Born, Chicago, Illinois, June, 1892; associated with Estate of Marshall Field, Real Estate Department; Director, Gordon Strong & Company; Director, Harvester Office Building Company; Chairman, Chicago Wholesale District Property Owners' Committee; Chairman, Albany Park Business Property Owners' Association; Director, Greater Central District Association; active member, Chicago Real Estate Board; professional territory covers Cook and Lake Counties, Illinois; attended The University of Chicago; fifteen years' experience in appraising real property, including stores, theatres and office buildings, industrial property, and special-purpose properties; licensed real estate broker in the state of Illinois since 1935; qualified in court as an expert on the valuation of commercial property.

HAROLD V. GLOS, CHICAGO, ILL.

Born, Wayne, Illinois, December, 1886; Appraiser and Manager, Property Sales and Property Management Departments, Sontag Bros., Inc.; active member, DuPage County Real Estate Board; professional territory covers principally Cook and DuPage Counties, Illinois; B.S. degree in mechanical engineering, Armour Institute of Technology, 1908; ten years' experience as Fire Protection Engineer with National Board of Fire Underwriters; four years' experience as a real estate broker and appraiser in Miami, Florida; ten years' experience as an appraiser and real estate broker in Chicago; fourteen years' experience in appraising real property, including the valuation of homes, apartments, stores, office buildings, industrial property, farms, and vacant property; licensed real estate broker in the state of Illinois from 1919 to 1923 and from 1927 to date; qualified in court as an expert on the value of multiple-unit apartment buildings; eighteen years' experience in residential sales.

VALENTINE B. HABRYL, CHICAGO, ILL.

Born, Chicago, Illinois, November, 1889; engaged in real estate appraising and the compilation of statistical data on office buildings; consultant on building valuations for the Building Managers' Association of Chicago; active member, Chicago Real Estate Board; professional territory covers Illinois, Wisconsin, and Michigan; assisted in compiling the Cook County Assessors' Manual for the 1928 Reassessment as superintendent in charge of building pricing; B.S. degree in electrical engineering, University of Illinois, 1912; statistician for the Property Owners' Committee on Subway Assessments; fifteen years' experience in appraising real property, including homes, apartments, stores, office buildings, industrial property, and special-purpose properties; licensed real estate broker in the state of Illinois since 1935; qualified in court as an expert on the value of commercial property; experienced in construction and in residential sales.

MALCOLM R. MAC DONALD, CHICAGO, ILL.

Born, Minneapolis, Minnesota, 1892; General

Partner, Preston M. Nolan and Company; active member, Chicago Real Estate Board; professional territory covers all states east of the Mississippi River; attended Dartmouth College, 1915; experienced in mortgage bond underwriting and subdivision development; property examiner for the Chicago Clearing House Association and the Reconstruction Finance Corporation; appraiser for Federal Public Works Administration; in charge of Appraisal Division for the United States Government covering all property in thirty-seven city blocks in Chicago; licensed real estate broker since 1930; qualified in court as an expert on the value of commercial, industrial, residential, and municipal properties; experienced in general building construction; ten years' experience in residential sales.

EUGENE E. MULHERN, CHICAGO, ILL.

Born, Boston, Massachusetts, May, 1886; real estate appraisal business under own name; also associated with Farnsworth & Mulhern, Real Estate Appraisers; employed since 1934 by the Estate of Marshall Field, appraising on a salary and also on a fee basis; Director, Rogers Park State Bank of Chicago; active member, Chicago Real Estate Board; professional territory covers metropolitan Chicago; attended St. Ignatius College (now Loyola University); eighteen years' experience in appraising real estate, including the valuation of homes, apartments, stores, and special-purpose properties; qualified in court as an expert on the value of residential property, 1922; licensed real estate broker; experienced in residential sales.

W. GORDON JOHNSTONE, DETROIT, MICH.

Born, Acton, Ontario, Canada, February 1895; Vice President, Houseman-Spitzley Corporation; Treasurer, Grayton Corporation; Treasurer, Pingree-Shreve Corporation; Treasurer, Medical Properties Corporation; member, Detroit Real Estate Board; professional territory covers Detroit, Grosse Pointe, and Bloomfield Hills; B.A. degree in engineering, University of Michigan, 1918; attended course in advanced real estate appraising, Wayne University; ten years' experience in appraising real property, including the valuation of homes, apartments, stores, office buildings, industrial property, vacant property, and special-purpose properties; twenty years' experience in selling, subdividing, building, managing, and mortgaging properties; licensed real estate broker since 1918; qualified in court as an expert on the value of real property; constructed approximately fifty residences and stores; sold more than five million dollars of private homes in Grosse Pointe and elsewhere.

PETER HOEK, GRAND RAPIDS, MICH.

Born, Grand Rapids, Michigan, August, 1874; employed by Home Owners' Loan Corporation since December, 1933; broker member, Grand Rapids Real Estate Board; alternate member, Grand Rapids Real Estate Board Appraisal Committee; State Appraiser, State and County Highway Department (Kent County); Vice President and Past President, Northwestern Improvement Association, Grand Rapids; professional territory covers the city of Grand Rapids, Kent County, Michigan, and also parts of western Michigan; fifteen years' experience as a real estate broker; seven years' experience in the appraising of real estate, including the valuation of residential, commercial, industrial, and farm properties; qualified in court as an expert on city, farm, and vacant property values in 1933; experienced in the construction and sale of residential property.

EDWARD M. THORNHILL, ST. LOUIS, MO.

Born, St. Louis, Missouri, July, 1889; Partner, Edward M. Thornhill & Son; member, St. Louis Real Estate Exchange; former Director and Treasurer, St. Louis Real Estate Exchange; professional territory covers St. Louis and St. Louis County; attended St. Joseph's College, Windsor Springs, Missouri; completed Case-Study Courses, Real Estate Appraisal I and II, 1935, and Condemnation Lecture Course, 1938, conducted by the American Institute of Real Estate Appraisers at The University of Chicago; ten years' experience in real estate appraising, including the valuation of homes, apartments, stores, industrial property, and special-purpose properties; qualified in court as an expert on the value of all types of real estate except office buildings; licensed real estate broker.

EDGAR H. BIXLER, ARLINGTON, N. J.

Born, Hanover, Pennsylvania, April, 1901; Manager, Edward A. Strong; President, Wilbix Realty and Construction Company; Past President, Arlington-Kearny Real Estate Board; President, Insurance Agents Association of West Hudson and North Arlington; Secretary, Kearny Chamber of Commerce; Past President, Kiwanis Club; Assistant Field Director for Extension Course, Real Estate Appraisal I, conducted by the Real Estate Board of Newark, Inc., and the New Jersey Chapter No. 1 of the American Institute of Real Estate Appraisers, 1938-39; pro-

fessional territory covers northern New Jersey; attended Gettysburg College, Pennsylvania State College, and Rutgers University Extension Course in appraising; completed Case-Study Courses, Real Estate Appraisal I and II, conducted by the American Institute of Real Estate Appraisers at Columbia University, 1937; ten years' experience in real estate appraising, including the valuation of homes, apartments, stores, office buildings, farms, and special-purpose properties; licensed real estate broker in the state of New Jersey since 1924; qualified in court as an expert on the value of real property; experienced in general construction work; fourteen years' experience in residential sales.

R. MASON KIRKLAND, ELIZABETH, N. J.

Born, Elizabeth, New Jersey, May, 1891; President, R. J. Kirkland & Son; Vice President and Director, Winfield Scott Hotel; individual member, The Institute of Real Estate Management; Past President, Elizabeth Real Estate Board; former Chairman, Appraisal Committee, Elizabeth Real Estate Board; Director, Elizabeth Chamber of Commerce for a number of years; professional territory covers Elizabeth, New Jersey, and vicinity; twenty years' experience in appraising real estate, including the valuation of industrial, vacant, commercial, residential, and acreage properties; qualified in court as an expert on the value of real property.

JAMES ROSENSOHN, ELIZABETH, N. J.

Born Passaic, New Jersey, December, 1900; President and Treasurer, James Rosensohn, Inc.; sales and management broker and independent fee appraiser, Home Owners' Loan Corporation; professional territory covers the state of New Jersey; broker member, Elizabeth Real Estate Board; individual member, The Institute of Real Estate Management; nine years' experience in the appraising of real estate, including the valuation of stores, theatres, lofts, office buildings, and multiple-family units; during 1926 to 1929 engaged in estimating building costs and as field superintendent of construction for the Rolo Company, Inc., general contractors, Newark; architectural training in office of Hyman Rosensohn, Architect; studied architecture, Columbia University; engaged in real estate activities since 1922; received technical real estate appraising at Rutgers University Extension Division.

WILLIAM CLIFFORD, JR., SHORT HILLS, N. J.

Born, Elizabeth, New Jersey, November, 1896; Mortgage Loan Inspector, Prudential Insurance Company; registered architect in New Jersey since 1921; associate member, Real Estate Board of Newark, Inc.; professional territory covers the state of New Jersey; seven years' experience in the appraisal of real estate, plus five years in building construction as superintendent and estimator; ten years as an architect; four years as district manager handling property management and sales for The Prudential Insurance Company of America and the New York Title Company; licensed real estate broker in the state of New Jersey.

RAYMOND S. DE MOTT, BRONXVILLE, N. Y.

Born, Cleveland, Ohio, June, 1897; President, DeMott Construction Company, Inc.; Director, New York Federal Savings & Loan Association; Vice President, Westchester Better Homes Exposition, Inc., 1937; member, Associated General Contractors of America; member, Westchester County Realty Board; professional territory covers Westchester County and some of metropolitan New York; graduate of the University of Michigan in engineering, 1921; eight years' experience in the appraisal of real property, including the valuation of residential properties and income properties; licensed real estate broker in the state of New York since 1928; licensed engineer in the state of New York.

ALFRED R. MARCKS, BROOKLYN, N. Y.

Born, New York, New York, August, 1902; Mortgage Officer, The Dime Savings Bank of Brooklyn; professional territory covers Kings, Queens, and Nassau Counties, New York; member, Brooklyn Real Estate Board; attended Pratt Institute; fourteen years' experience in the appraisal of real property, including apartments and warehouses; licensed real estate broker in the state of New York, 1925-1939; qualified in court as an expert on the value of vacant land in 1934.

D. DUFFY LANE, ELMHURST, N. Y.

Born, Bucharest, Rumania, January, 1900; Secretary, Frank O'Hara, Inc., Jackson Heights, New York; formerly Vice President, Weber & Merritt, Inc.; member, American Society of Heating and Ventilating Engineers; nonbroker member, Long Island Real Estate Board; professional territory covers Kings, Queens, and Nassau Counties, New York; attended City College of New York and appraisal course at New York University; ten years' experience in real estate appraising, including the valuation of homes, apartments, stores, vacant land, and industrial property; licensed real estate salesman in the

state of New York; qualified in court as an expert on the value of apartment houses, 1936; experienced as a general builder and supervisor of building construction; experienced in residential sales.

HENRY F. LINSMANN, MOUNT VERNON, N. Y.

Born, New York, New York, March, 1890; Chief Valuator, Federal Housing Administration, White Plains, New York, 1936 to date; Chief Appraiser, Home Owners' Loan Corporation, White Plains, 1933-1935; with the Irving Trust Company for nineteen years, of which eleven were in Mortgage and Real Estate Departments; with State Title and Mortgage Company for four years; associate member, Westchester County Realty Board; professional territory covers Bronx, Westchester, Putnam, Dutchess, Rockland, Orange, Ulster, and Sullivan Counties, New York; attended real estate and appraising courses at New York University; completed Case-Study Course, Real Estate Appraisal II, conducted by the American Institute of Real Estate Appraisers at Columbia University, 1937; fifteen years' experience in the appraising of real property; three years' experience as real estate broker.

EDWIN F. ARMSTRONG, NEW YORK, N. Y.

Born, New York, New York, November, 1904; Partner, Armstrong & Armstrong; Secretary, John Armstrong Estate, Inc.; Trustee, Estate of Robert J. Armstrong; member, Manhattan Chapter, National Association of Real Estate Boards; professional territory covers New York City and Westchester County; three years at Columbia College and one year at School of Business, Columbia University; eight years' experience in the appraisal of real property, including the valuation of apartments, vacant land, homes, loft buildings, and other types of real estate in metropolitan New York City; licensed real estate broker in the state of New York; qualified in court as an expert on the value of investment and residential property, 1932.

HERBERT R. HOUGHTON, NEW YORK, N. Y.

Born, New York, New York, January, 1888; senior member, Houghton Company; President Westchester County Realty Board; member, License Law Committee, The Real Estate Association of the State of New York; professional territory covers New York City and Westchester County; ten years' experience in real estate appraising, including the valuation of homes, apartments, stores, and office buildings; qualified in court as an expert on the value of residential property, 1929; licensed real estate broker in the state of New York; thirty years' experience in residential sales.

LAURENCE H. LANG, CLEVELAND, O.

Born, Cleveland, Ohio, June, 1897; owner, real estate management and brokerage office under own name; professional territory covers northern Ohio and some chain-store activity throughout the Middle West; member, Cleveland Real Estate Board; B.A. degree, Williams College; completed the Extension Course, Real Estate Appraisal I, at Cleveland, 1938, and Case-Study Course, Real Estate Appraisal II, at The University of Chicago, 1938, conducted by the American Institute of Real Estate Appraisers; appraisal experience includes the valuation of apartment properties, single-family homes, stores, vacant lots, industrial property, and churches.

SIDNEY EISENBERGER, DAYTON, O.

Born, Dayton, Ohio, November, 1885; President, Eiber Realty Company; local property manager, New York Life Insurance Company; active member, Dayton Real Estate Board; professional territory covers the Middle West; student in Case-Study Course, Real Estate Appraisal II, conducted by the American Institute of Real Estate Appraisers at The University of Chicago, 1935; seventeen years' experience in appraising real property, including the valuation of homes, apartments, stores, office buildings, industrial property, farms, and numerous special-purpose properties; licensed real estate broker in the state of Ohio since 1919; qualified in court as an expert on the valuation of theatre, mercantile, residential, and vacant properties; experienced in residential construction and sales.

ELMER H. SEIDMAN, LAKEWOOD, O.

Born, Cleveland, Ohio, January, 1894; Treasurer and Director, The West Side Realty Company; Trustee, Cleveland Real Estate Board; professional territory covers metropolitan Cleveland; completed Case-Study Course, Real Estate Appraisal II, conducted by the American Institute of Real Estate Appraisers at Columbia University, 1937, and Extension Course, Real Estate Appraisal I, in Cleveland, 1938; B.L. degree, Baldwin Wallace University, 1915; eighteen years' experience in appraising real estate, including the valuation of homes, apartments, stores, industrial property, farms, and numerous special-purpose properties; licensed real estate broker in the state of Ohio; qualified in court as an expert on real

estate values; ten years' experience in the supervision of residential and commercial construction; twenty-three years' experience in residential sales.

F. C. McGOWAN, PORTLAND, ORE.

Born, Eau Claire, Wisconsin, March, 1877; proprietor, Fred C. McGowan, Realty Counselors; President and Director, Union Bond & Trust Company; Vice President and Director, Evergreen Lumber Company; professional territory covers Oregon and southern Washington; Past President, Portland Realty Board; Vice President and Director, Portland Federal Savings & Loan Association; Vice President and Director, United States Building & Loan Association; B.L. degree, University of Wisconsin; appraisal experience from 1918-1925 and 1929-1938, including the valuation of homes, farms, industrial property, and business property; licensed real estate broker in the state of Oregon since 1929; qualified in court as an expert on the value of industrial property, farms, and residential property; experienced in residential sales since 1907.

W. H. ROSS, PORTLAND, ORE.

Born, Bloomington, Illinois, May, 1874; President, Ross & Marks, Inc.; active member, Portland Realty Board; professional territory covers Oregon and Washington; author and lecturer; attended University of Oregon, two years; twenty years' experience in appraising real estate, including homes, apartments, stores, office buildings, farms, industrial property, and theatres; licensed real estate broker in the state of Oregon; qualified in court as an expert on the value of industrial and farm properties; experienced in the construction of homes, stores, and apartment properties; twenty years' experience in residential sales.

ALBERT H. LIEBERMAN, PHILADELPHIA, PA.

Born, Lida, Russia, May, 1886; President, Albert H. Lieberman, Inc.; Secretary and Managing Director of many building and loan associations; Treasurer, Swarthmore Realty Corporation; active member, Philadelphia Real Estate Board; professional territory covers Philadelphia and suburbs, eastern Pennsylvania, and New Jersey; took special courses at the University of Pennsylvania; twenty-eight years' experience in the appraising of real property, including the valuation of homes, apartments, stores, office buildings, industrial property, farms, and special-purpose properties; licensed real estate broker in Pennsylvania; many years' experience in building and construction, also residential sales.

ALBERT O. HORNER, PITTSBURGH, PA.

Born, Mount Pleasant, Pennsylvania, August, 1879; Partner, Horner & Daubenspeck; President and Director, Home Mutual Building & Loan Association; Treasurer and Director, North Hills Land & Improvement Company; member, Pittsburgh Real Estate Board; professional territory covers Allegheny County, Pennsylvania; graduate, Juniata College, Huntingdon, Pennsylvania, 1899; graduate, Duff's Business College, Pittsburgh, 1900; Past President, Allied Boards of Trade; Past President, North Side Chamber of Commerce; member, Planning Commission, city of Pittsburgh, more than eight years; Past President, Allegheny County Building & Loan League; Director, United States Building & Loan League, 1933-1935; twenty-five years' experience in the appraising of real property; licensed real estate broker in the state of Pennsylvania; qualified in court as an expert on the value of residential land and business property; some building and construction experience; residential sales experience since 1900.

DONNELL D. REED, PITTSBURGH, PA.

Born, Pittsburgh, Pennsylvania, December, 1897; Property Assessor, city of Pittsburgh; professional territory covers city of Pittsburgh; active member, Pittsburgh Real Estate Board; graduate, Carnegie Institute of Technology, in building construction, 1917; graduate, real estate appraisal course given by the University of Pittsburgh, 1934; completed Case-Study Courses, Real Estate Appraisal I and II, and also Condemnation Lecture Course conducted by the American Institute of Real Estate Appraisers at The University of Chicago, 1938; superintendent and chief estimator of various types of building construction for fifteen years; fifteen years' experience in real estate appraising; licensed real estate broker in the state of Pennsylvania; qualified in court as an expert on the value of real property.

FRED B. WETZEL, WILLIAMSPORT, PA.

Born, Williamsport, Pennsylvania, October, 1896; President, Fred B. Wetzel, Inc.; Past President, Williamsport Real Estate Board; individual member, The Institute of Real Estate Management; sixteen years' experience in real estate brokerage, subdividing, construction, and financing of residential real estate; fee appraiser, Home Owners' Loan Corporation; qualified in court as an expert on the value of real estate.

LOUIS A. WETZEL, WILLIAMSPORT, PA.

Born, Williamsport, Pennsylvania, November, 1906; President, Wetzel-Rider Company; Secretary, Williamsport Federal Savings & Loan Association; Director, Penn Central Mortgage Corporation; Director, Faxon Lumber Company; Director, Faxon Construction Company; member, Williamsport Real Estate Board; professional territory covers Williamsport and vicinity, Lycoming County, Clinton County, and Union County; one year at Williamsport Commercial College; completed Case-Study Courses, Real Estate Appraisal I and II, 1936, and the Condemnation Lecture Course, 1938, conducted by the American Institute of Real Estate Appraisers at The University of Chicago; eight years' experience in appraising real property, including the valuation of homes, apartments, stores, office buildings, industrial property, farms, and special-purpose properties; licensed real estate broker in the state of Pennsylvania; qualified in court in 1934 as an expert on the value of residential property; thirteen years' experience as general contractor; thirteen years' experience in residential sales.

LEO V. BOYLE, PAWTUCKET, R. I.

Born, Woonsocket, Rhode Island, April, 1886; Past President, Director, and Chairman of all committees at different times during the past seventeen years of the Pawtucket Real Estate Exchange; Past President and Director, Chamber of Commerce and Business Men's Association of Pawtucket; Chairman, Industrial Development Committee; professional territory covers Pawtucket, Providence, and cities and towns within a radius of ten miles thereof; attended Brown University, Rhode Island School of Design, Boston University, and Pace & Pace School of Accountancy & Finance; seventeen years' experience in the appraising of real estate, including appraisals of leaseholds, stores, tenements, cottages, vacant land, apartment properties, houses, and hotels; qualified in court as an expert on the value of real property; seventeen years' experience in real estate sales.

WILHELMINE B. SHEFFIELD, AUSTIN, TEX.

Born, Austin, Texas, February, 1900; Manager, Real Estate Department, Millican & Hamby, doing a general brokerage, appraising, and management business; individual member, National Association of Real Estate Boards; attended University of Texas; completed Case-Study Courses, Real Estate Appraisal I and II, conducted by the American Institute of Real Estate Appraisers at The University of Chicago, 1935; completed Case-Study Courses, Real Estate Management I and II, conducted by The Institute of Real Estate Management at The University of Chicago, 1936; lecturer and instructor; eleven years' experience in appraising real estate, including the valuation of homes, vacant lots, store properties, hotels, schools, and churches.

CHARLES W. CART, SAN ANTONIO, TEX.

Born, Versailles, Kentucky, August, 1896; Director and Secretary-Treasurer, First Federal Savings & Loan Association of San Antonio; Director and Secretary-Treasurer, Security Building & Loan Association; member, San Antonio Real Estate Board; professional territory covers San Antonio and environs; appraiser, Home Owners' Loan Corporation since 1936; fifteen years' experience in the appraising of real property.

HARRY C. MILLER, WHEELING, W. VA.

Born, Jewett, Ohio, June, 1888; Secretary-Treasurer, The Wheeling Realty Company; Past President, Wheeling Real Estate Board; Past President, West Virginia Real Estate Association; professional territory covers the entire Wheeling metropolitan district; appointed Fee Appraiser, Home Owners' Loan Corporation, 1933; appraised properties for the West Virginia State Banking Commission; twenty-one years' experience in appraising real estate, including the valuation of dwellings, apartments, hotels, commercial buildings, and public utilities; qualified in court as an expert on the value of real property; licensed real estate broker in West Virginia since 1909 and in Ohio since 1926.

KENNETH E. SARLES, RACINE, WIS.

Born, Spokane, Washington, May, 1907; President, Racine Property Service, Inc.; Appraiser, Home Owners' Loan Corporation; Appraiser for Racine County in condemnation cases; member, Racine Real Estate Board; professional territory covers the state of Wisconsin; three years, College of Agriculture, University of Wisconsin; one year at Madison Business College, studying commercial law; one year of study in general law; nine years' experience in appraising real property, including the valuation of farms, residential property, filling stations, stores, and office buildings; qualified in court as an expert on the value of real property; licensed real estate broker in the state of Wisconsin; ten years' experience in residential sales.

1939 OFFICERS OF AMERICAN INSTITUTE OF REAL ESTATE APPRAISERS

THE PRESIDENT

Ralph V. Field
203 Bank of Galesburg Bldg., Galesburg, Illinois

VICE PRESIDENTS

Wm. H. Ballard.....New England Region
45 Milk Street, Boston, Massachusetts

Charles B. Shattuck.....Southwest Region
2510 S. Vermont Avenue, Los Angeles, Calif.

Warren L. Morris.....Great Lakes Region
825 Nat. City Bk. Bldg., Cleveland, Ohio

Maurice R. Massey.....Central Atlantic Region
S.E. Corner 13th and Green Streets
Philadelphia, Pennsylvania

William A. Eastman.....Northwest Region
414 University Street, Seattle, Washington

Reginald W. Patton.....South Central Region
621 Travis Building, San Antonio, Texas

John B. Green.....Southeast Region
11 Fourth Street, N., St. Petersburg, Florida

Lewis C. Sholes.....North Central Region
Care of County Assessor, Court House
Omaha, Nebraska

Herbert U. Nelson.....Secretary
22 West Monroe Street, Chicago, Illinois

Charles S. Wanless.....Treasurer
319 South Fifth Street, Springfield, Illinois

Harry Grant Atkinson.....Director of Activities
22 West Monroe Street, Chicago, Illinois

GOVERNING COUNCIL

Term Expiring December 31, 1941

James W. Cree, Jr., Pittsburgh, Pennsylvania
George W. Drennan, Detroit, Michigan
Newton C. Farr, Chicago, Illinois
Ralph V. Field, Galesburg, Illinois
J. Burrows Johnson, New Orleans, Louisiana
Stanley C. Hanks, Madison, Wisconsin
Maurice R. Massey, Philadelphia, Pennsylvania
Frank M. McCurdy, Brooklyn, New York
George L. Schmutz, Los Angeles, California

Term Expiring December 31, 1940

Ralph D. Baker, Camden, New Jersey
William H. Ballard, Boston, Massachusetts
William W. Butts, St. Louis, Missouri
William A. Eastman, Seattle, Washington
Hill Ferguson, Birmingham, Alabama
Arthur C. Houghton, Washington, D. C.
David Neiswanger, Topeka, Kansas
Reginald W. Patton, San Antonio, Texas
Charles B. Shattuck, Los Angeles, California

Term Expiring December 31, 1939

Frederick M. Babcock, Washington, D. C.
John B. Green, St. Petersburg, Florida
John R. Hoyt, New York, New York
Edward J. Maier, Newark, New Jersey
Frank McLaughlin, Toronto, Ontario
Warren L. Morris, Cleveland, Ohio
Lewis C. Sholes, Omaha, Nebraska
Morton G. Thalhimer, Richmond, Virginia
H. O. Walther, Chicago, Illinois

Past Presidents on the Governing Council

Philip W. Kniskern, Philadelphia, Pennsylvania
(Term Expiring December 31, 1939)

Joseph B. Hall, Cleveland, Ohio
(Term Expiring December 31, 1940)

Harry E. Gilbert, Baltimore, Maryland
(Term Expiring December 31, 1940)

Maurice F. Reidy, Worcester, Massachusetts
(Term Expiring December 31, 1941)

E. L. Ostendorf, Cleveland, Ohio
(Term Expiring December 31, 1942)

K. Lee Hyder, Milwaukee, Wisconsin
(Term Expiring December 31, 1943)

Representing Board of Directors, N.A.R.E.B.

Paul E. Stark, Madison, Wisconsin

1939 COMMITTEES

STANDING COMMITTEES

(See pages 188 to 193, "Roster of Members," for addresses.)

ADMISSIONS COMMITTEE

Warren L. Morris, Cleveland, O., *Chairman*
Stanley Roe, Chicago, Ill., *Chairman, Subcommittee on Examinations*
George C. Sexauer, *Chairman, Subcommittee on Reports*
Boyd T. Barnard, Philadelphia, Pa.
Fritz W. Beck, Milwaukee, Wis.
Henry B. Bunker, Cincinnati, O.
Fred L. Chapman, Washington, D. C.
Preston Cooke, Columbus, O.
Edward J. Crawford, New York, N. Y.
C. F. Curry, Kansas City, Mo.
W. E. Ferguson, Baltimore, Md.
Morris Goldfarb, Perth Amboy, N. J.
George H. Gray, Brooklyn, N. Y.
W. G. Harris, Los Angeles, Calif.
Meredith H. James, Houston, Tex.
J. Burrows Johnson, New Orleans, La.
Werner Kiepe, Salt Lake City, Ut.
Arthur Kruggel, Chicago, Ill.
Henry E. Reed, Portland, Ore.
Paul F. Semonin, Sr., Louisville, Ky.
Walter D. Shelly, Jacksonville, Fla.
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George W. Drennan (358).....617 Penobscot Bldg.
Guy S. Greene (394).....300 Lafayette Bldg.
Donald D. James (539).....700 Penobscot Bldg.
Henry N. Johnson (390).....300 Penobscot Bldg.
W. Gordon Johnstone (700).....1400 United Artists Bldg.
Albert D. MacRae (640).....Union Guardian Bldg.
Arthur A. May (686).....950 Nat. Bk. Bldg.
Alfred W. Palmer (312).....1920 Union Guardian Bldg.
Edmund T. Paterson (385).....3050 E. Grand Blvd.
Leonard P. Reaume (393).....2150 Buhl Bldg.
George C. Sexauer (395).....2150 Buhl Bldg.
William W. Tanney (434).....9061 W. Outer Dr.
Ward S. Van Deusen (665).....705 Fidelity Bldg.
Clarence S. Vaughn (422).....2103 First Nat. Bk. Bldg.
Carl S. Wells (391).....2706 Eaton Tower

Flint
Gerald F. Healy (604).....611 Genesee Bk. Bldg.

Grand Rapids
Isaac R. Blandford (234).....105 Federal Square Bldg.
Leon T. Closterhouse (247).....Central Bk.
John Garfield Emery (304).....400 Central Bk. Bldg.
Harry J. Fuller (235).....The Michigan Tr. Co.
Peter Hoek (713).....750 Leonard St., N. W.
Walter S. Palmer (193).....104 Federal Sq. Bldg.
Arent Van Stensel (248).....701 Peoples Nat. Bk. Bldg.
Charles H. Warden (229).920 Grand Rapids Nat. Bk. Bldg.

Jackson
Henry H. Lammers (557).....508 Dwight Bldg.

Lansing
Edward G. Hacker (291).....221½ W. Washtenaw St.

Pontiac
Paul A. Kern (134).....31 Oakland Ave.

MINNESOTA

Duluth
Richard W. Northrup (379).....600 Torrey Bldg.

Minneapolis
Norman L. Newhall (32).....519 Marquette Ave.
Edwin L. Somerville (30).....519 Metropolitan Bk. Bldg.
J. Frederick Sutherland (331).....Suite 450, Baker Bldg.

MISSISSIPPI

Jackson
J. O. Manning (299).....3012 N. State St.

MISSOURI

Clayton
Gunther Meier (319).....24 N. Meramec Ave.

Joplin
Rolla E. Stephens (264).....711 Virginia Ave.

Kansas City
George M. Bliss (360).....17 E. Tenth St.
C. F. Curry (345).....921 Baltimore Ave.
Ward C. Gifford (667).....709 Nat. Fidelity Life Bldg.
Herbert B. Patt (553).....417 R. A. Long Bldg.
E. F. Pierson (289).....311 Commerce Bldg.

St. Louis
W. C. Bernard (91).....412 City Hall
William W. Butts (93).....410 Wainwright Bldg.
Herbert O. Byrd (302).....818 Chestnut St.
Charles J. Daly (94).....801 Chestnut St.
Otto J. Dickmann (225).....804 Chestnut St.
Chester A. Dougherty (249).....109 N. Seventh St.
J. Gregory Driscoll (528).....1501 Locust St.
John H. Farish (201).....713 Chestnut St.
Grover Godwin (418).....1796 Arcade Bldg.
Joseph W. Hannauer (15).....811 Chestnut St.
Alfred B. Kissack (525).....915 Olive St.
Curt C. Mack (449).....F.H.A.
Francis A. Reardon (668).....111 N. Tenth St.
Monroe H. Rodemyer (218).....109 N. Eighth St.
Edward M. Thornhill (693).....807 Chestnut St.
N. S. Wood (131).....709 Chestnut St.

NEBRASKA

Lincoln
C. C. Kimball (381).....Stuart Bldg.
W. B. Romans (669).....2841 Rathbone Rd.

Omaha
Lewis C. Sholes (23)..Care of County Assessor, Court House
Clinton B. Stuht (33).....Aquila Court Bldg.

NEW JERSEY

Arlington
Edgar H. Bixler (701).....100 Midland Ave.

Atlantic City
Maurice A. Kelley (325).....20 S. Tennessee Ave.

Bayonne
George Seymour (670).....9 W. Eighth St.

Butler
Frank B. Fay, Jr. (171).....Fayson Lake

Camden
Ralph D. Baker (60).....924 Broadway
William W. Chalmers (63).....645 Market St.
Abraham J. Rosenfeld (213).....300 Broadway
Leon E. Todd (340).....2623 Westfield Ave.
Philip Zinman (95).....643 Market St.

East Orange
Frank H. Taylor (6).....520 Main St.
Harry A. Taylor (108).....520 Main St.

Elizabeth
John P. Gloeckner (655).....1143 E. Jersey St.
R. Mason Kirkland (714).....125 Broad St.
John K. Leeds (99).....286 N. Broad St.
B. B. Miller (58).....215 Broad St.
James Rosensohn (715).....125 Broad St.
Burton Thompson (43).....18 W. Jersey St.
Max Tieger (112).....207 Broad St.

Jersey City
Percy A. Gaddis (22).....900 Bergen Ave.
D. E. C. Somers (175).....700 Bergen Ave.
R. E. Thompson (419).....Centl. R. R. of N. J. Term.

Linden
John Fedor (65).....540 S. Wood Ave.

Maplewood
Gilbert N. Swett (561).....Depot Plaza

Newark
Murray Apfelbaum (38).....17 William St.
John J. Berry (56).....982 Broad St.
George E. Dugan (236).....18 Washington Pl.
Charles F. Evans (572).....782 S. 19th St.
Joseph L. Feibleman (66).....17 Academy St.
George Goldstein (413).....810 Broad St.
Franklin Hannoch (49).....14 Park Pl.
Louis Herman (70).....60 Park Pl.
Charles Frederick Kraemer (366).....776 Broad St.
Rudolph Kruger (516).....11 Hill St.
John A. Linnett (85).....46 Clinton St.
E. J. Maier (75).....187 Market St.
Joseph L. Pitman (661).....60 Park Pl.
Joel L. Schlesinger (87).....31 Clinton St.
Harry J. Stevens (200).....478 Central Ave.

New Brunswick
James A. O'Connell (186).....392 George St.

Newton
A. N. Lockwood (433).....17 Main St.

Ocean City
Elmer Jackson Pearl (330).....810 Ocean Ave.

Paterson
Joseph R. Lambert (443).....20-22 Church St.

Perth Amboy
Morris Goldfarb (109).....265 Madison Ave.

Plainfield
Milton Brown (662).....131 North Ave.
William G. McDowell (446).....152 North Ave.

Ridgewood
Frederick A. Tetor (364).....1 E. Ridgewood Ave.
Samuel S. Walstrum (106).....201 E. Ridgewood Ave.

Rutherford
Charles A. Van Winkle (113).....1 & 2 Station Sq.
Theodore Van Winkle (117).....1 & 2 Station Sq.

Short Hills
William Clifford, Jr. (716).....87 Whitney Rd.

NEW MEXICO

Albuquerque
Joseph P. Deasy (377).....1106 Virginia Blvd.

NEW YORK

Buffalo
A. P. Allingham (3).....158 Pearl St.
P. V. Bowen (141).....1006 Ellicott Sq.
Walter W. Cohn (81).....155 Pearl St.
Cuthbert E. Reeves (19).....Liberty Bank Bldg.

Mechanicville
Franz H. Moak (40).....37 N. Main St.

Metropolitan City of New York

Borough of Bronx

Herman A. Acker (279).....318 E. Kingsbridge Rd.
Amedeo Giordano (515).....2488 Grand Concourse
Samuel E. McRickard (292).....400 E. Fordham Rd.

Borough of Brooklyn

Stephen F. Barrera (133).....191 Joralemon St.
George Baur (170).....2609 Clarendon Rd.
Charles D. Behrens (635).....190 Montague St.
Joseph William Catharine (503).....149 Pierrepont St.
James P. Clark (550).....478 Graham Ave.
James B. Fisher (57).....160 Remsen St.
George H. Gray (17).....310 Ashland Pl.
Bernard F. Hogan (29).....451 Fifth Ave.
Arthur J. Horton (183).....6904 Fourth Ave.
George S. Horton (184).....59 Lafayette Ave.
Alfred R. Marcks (718).....9 DeKalb Ave.
James F. Matthews (76).....186 Joralemon St.
Frank M. McCurdy (39).....44 Court St.
M. C. O'Brien (190).....798 Nostrand Ave.
Charles Partridge (92).....397 Flatbush Ave.
Lewis H. Pounds (128).....32 Court St.
Milton T. VanderVeer (660).....51 Willoughby St.
R. W. Walden (89).....141 Montague St.
Alfred R. Wittich (649).....99 Pennsylvania Ave.

Borough of Manhattan

Edwin F. Armstrong (702).....485 Madison Ave.
Robert H. Armstrong (562).....485 Madison Ave.
Edward J. Crawford (373).....225 Broadway
Dalton Granger De Witt (315).....22 W. 48th St.
Sam W. Florence (206).....2700 Woolworth Bldg.
Howard Geoghegan (512).....51 Chambers St.
A. N. Gitterman (45).....45 E. 49th St.
James A. Glynn, Jr. (671).....100 E. 42nd St.
Bracton Goldstone (68).....10 E. 40th St.
George Grotz, Jr. (573).....100 E. 42nd St.
George M. Halk, Jr. (582).....742 Lexington Ave.
Frank D. Hall (159).....393 Seventh Ave.
Herbert R. Houghton (703).....12 E. 41st St.
John R. Hoyt (290).....17 E. 42nd St.
Robert Huntley (214).....67 Liberty St.
S. E. Kazdin (269).....70 Pine St.
Harry K. Keller (563).....522 Fifth Ave.
John J. McCormick (445).....51 Chambers St.
Thomas E. McSherry (636).....51 Chambers St.
Clarence C. Merritt (357).....50 E. 42nd St.
Charles W. Morrison (270).....270 Madison Ave.
James R. Murphy (437).....217 Broadway
Henry Musch, Jr. (157).....270 Broadway
Charles A. Nehring (521).....1441 St. Nicholas Ave.
Charles J. Pladwell (542).....522 Fifth Ave.
Edmund J. Port (688).....17 E. 42nd St.
George Stanley Potter (656).....270 Madison Ave.
J. Kingsley Powell (77).....34 Nassau St.
Andrew B. Rankin (625).....160 Broadway
Irving I. Rosenbaum (179).....384 Broadway
I. Lincoln Seide (526).....220 Broadway
Maurice R. Spear (543).....225 Fifth Ave.
Eldridge C. Thompson (583).....34 Nassau Street
John C. Tredwell (574).....Rm. 1501, 393 Seventh Ave.
Wallace Whittington True (647).....393 Seventh Ave.
David Vogel (368).....150 Broadway

Borough of Queens

Armand Brunswick (327).....90-26 161st St., Jamaica
D. Duffy Lane (711).....87-65 52nd Ave., Elmhurst
William F. MacDermott (198).....89-70 162nd St., Jamaica
Axel J. Swenson (272).....41-27 29th St., Long Island City

Nassau County, Long Island

Richard T. Childs (273).....222 Front St., Mineola

Westchester County

Robert A. Anderson (259).....34 E. First St., Mt. Vernon

Stephen L. Angell (220).....30 E. Parkway, Scarsdale
Vernon N. Bailey (322).....175 Main St., White Plains
Raymond S. DeMott (717).....Pondfield Rd., Bronxville
Edward C. Heald (222).....20 S. Broadway, Yonkers
Edward H. Hufnagel (250)..100 Stevens Ave., Mt. Vernon
Henry F. Linsmann (719).....
.....126 Burkewood Rd., Mt. Vernon
Albert W. Lockyer (294).....Depot Plaza, White Plains
Paul Wegener (90).....144 S. Broadway, Yonkers
Edward M. West (305).....1 Martine Ave., White Plains

Rochester
Warren W. Allen (637)....Lincoln-Alliance Bk. & Tr. Co.
Linus S. Appleby (689).....183 Main St., E.
Abraham Berghash (219).....130 Clinton Ave., S.

Schenectady
William Garner Bee (415).....277 State St.

Syracuse
James H. Dawley (333).....121 E. Genesee St.
Edward Eagan (271).....204 Starrett-Syracuse Bldg.

NORTH CAROLINA

Charlotte
S. T. Henderson (20).....P. O. Box 965

OHIO

Akron
Charles S. Jenkins (564).....659 Schiller Ave.
John C. Kyle (102).....520 S. Firestone Blvd.
E. L. Marting (672).....27 S. High St.
A. R. Ritzman (544).....1099 S. Main St.
Eugene K. Sheffield (575).....651 Central Tower Bldg.
Fred E. Smith (298).....608 Broad Blvd., Cuyahoga Falls
W. F. Voges (105).....1109 S. Main St.

Canton
Mark Hambleton (146).....417 Mellett Bldg.
A. Ray Walters (439).....524 Renkert Bldg.

Cincinnati
Henry B. Bunker (545).....S. E. Cor. Fourth & Vine Sts.
Howard R. Burgess (176).....304 Neave Bldg.
Fred Droege, Jr. (154).....410 First Nat. Bk. Bldg.
J. George Ege (335).....3040 Urwiler Ave.
James W. Farrell (149).....S. W. Cor. Fifth & Main Sts.
James J. Grogan (180).....S. W. Cor. Fifth & Main Sts.
Albert J. Mayer (204).....1515 First Nat. Bk. Bldg.
P. Lincoln Mitchell (181)....S. W. Cor. Fifth & Main Sts.
Michael J. O'Byrne (429)....3270 Menlo Ave., Hyde Park
Russell Price (152).....S. W. Cor. Fifth & Main Sts.
Walter S. Schmidt (111)...S. W. Cor. Fifth & Main Sts.
Lewis R. Smith (139).....409 American Bldg.
John B. Spilker (155).....410 First Nat. Bk. Bldg.

Cleveland
Talmage D. Auble (262).....15509 Madison Ave.
Robert F. Berwald (300).....1220 Williamson Bldg.
Ben B. Beyer (34).....1425 Williamson Bldg.
James G. Bingham (328).....1227 Williamson Bldg.
Raymond T. Cragin (282).....825 Nat. City Bk. Bldg.
W. J. Crawford, Jr. (323).....720 Cuyahoga Bldg.
Victor J. Free (431).....P. O. Box 5876
Walter R. Granger (285).....310 Hippodrome Bldg.
Joseph J. Haas (164).....200 Marshall Bldg.
Joseph B. Hall (2).....5700 Truscon Ave.
Harry D. Knowlton (673).....920 Guardian Bldg.
Laurence H. Lang (694).....1101 Citizens Bldg.
Joseph Laronge (103).....600 Union Commerce Bldg.
Edwin H. McIntosh (283)....325 Society for Savings Bldg.
Warren L. Morris (251).....825 Nat. City Bk. Bldg.
C. A. Mullenix (605).....620 Hickox Bldg.
E. L. Ostendorf (14).....610 Nat. City Bk. Bldg.
Carl A. Palmer (286).....850 Euclid Ave.
L. R. Reifsnider (638).....944 Union Commerce Bldg.
Max J. Rudolph (281).....1105 Chester Ave.
Carlton Schultz (37).....The B. F. Keith Bldg.
Alexander S. Taylor (142)....1930 Union Commerce Bldg.
V. C. Taylor, II (153).....1930 Union Comerce Bldg.
William J. Van Aken (284).....1715 Euclid Ave.

Columbus
Preston Cooke (551).....8 E. Broad St.
Charles F. Johnson (412).....8 E. Long St.

Dayton
Sidney Eisenberger (704).....286 Fourth St. Arcade
Rufus Lisle (438).....704 Harries Bldg.

Geneva
J. Earl Miller (267).....Miller Bldg.

Lakewood
Elmer H. Seidman (705).....14802 Madison Ave.

Massillon
Charles N. Hostetter (329).....716 Lincoln Way, E.

Springfield
H. S. Kissell (5).....927 First Nat. Bk. Bldg.

Toledo
Claude A. Campbell (211).....707 Ohio Bk. Bldg.
Edmund T. Collins (522).....708 Jefferson Ave.
George P. Crosby (252).....413 Madison Ave.
Howard Etchen (136).....725 Adams St.
Donald F. Hiett (396).....622 Jefferson Ave.
John R. Schackne (529)....507 Produce Exchange Bldg.

OKLAHOMA

Tulsa
J. M. Allen (546).....Beacon Bldg.
Clyde A. King (432).....520 Beacon Bldg.

OREGON

Portland
Arthur C. Callan (674).....320 Oregon Bldg.
Merle G. Campbell (675).....511 Corbett Bldg.
Leroy D. Draper (676).....236 S. W. Broadway
James R. Haight (677).....408 S. W. Fourth Ave.
F. C. McGowan (706).....603 Couch Bldg.
Henry Edward Reed (678).....805 Title & Tr. Bldg.
W. H. Ross (707).....413 S. W. Stark St.
Nat C. Soule (679).....1112 Porter Bldg.
A. G. Teepe (690).....3114 N. E. Sandy Blvd.
Donald L. Woodward (680).....236 S. W. Broadway

PENNSYLVANIA

Bethlehem
William C. Bader (163).....214 Odd Fellows Bldg.

Erie
Carl G. Wright (361).....204 Marine Bk. Bldg.

Harrisburg
Evan J. Miller (148).....213 Locust St.

Lancaster
Harry W. Butts (114).....24 E. Orange St.

Lansdowne
W. Raymond Evans (118).....19 N. Lansdowne Ave.

Lewistown
E. Dale Fisher (520).....136 Valley St.

Philadelphia
Philip N. Arnold (174).....123 S. Broad St.
Boyd T. Barnard (237).....Lincoln-Liberty Bldg.
Frederick A. Bond (380).....5433 Baltimore Ave.
E. L. Carlson (62).....The Parkway at Fairmont Ave.
C. Harris Colehower (145).....5942 Chestnut St.
Frank P. Felton, Jr. (268).....914 Lincoln-Liberty Bldg.
Lionel Friedmann (565)....N.E. Cor. 15th & Locust Sts.
Joseph J. Greenberg (606).....Architects Bldg.
Samuel T. Hall (257).....1500 Locust St.
Roy A. Heymann (362).....213 S. Broad St.
C. Harry Johnson (238).....Packard Bldg.
S. Craig Kane, Jr. (253).....502 Land Title Bldg.
John G. Keck (607).....1622 N. Broad St.
Philip W. Kniskern (1).....1604 Walnut St.
Albert H. Lieberman (726)....N.W. Cor. 15th & Locust Sts.
J. William Markeim (86).....1424 Walnut St.
Frank H. Massey (549).....S. E. Cor. 13th & Green Sts.
Maurice R. Massey (276)....S. E. Cor. 13th & Green Sts.
J. Howard McLaughlin (372).....5512 Florence Ave.
William I. Mirkil (226).....1500 Walnut St.
Robert J. Nash (254).....1214 Locust St.
Glyndon Priestman (420).....18 W. Chelten Ave.
Richard J. Seltzer (255).....15th & Locust Sts.
J. Willison Smith (239).....100 S. Broad St.
Martin Stotz (55).....514 Land Title Bldg.
Joseph W. Widing (648).....1500 S. Broad St.
Philip O. Widing (639).....1604 Walnut St.
Ambrose J. Winder (207).....1420 Walnut St.

Pittsburgh
Roy R. Cappe (608).....341 Fourth Ave.
H. Chidester (609).....618 Frick Bldg.
James W. Cotts (610).....307 Fourth Ave.
James W. Cree, Jr. (13).....211 Fourth Ave.
E. Herbert Gilg (552).....6605 Ridgeville St.
Fred J. Hettling (611).....820 Grant Bldg.
Albert O. Horner (720).....12 N. Diamond St.
Carl E. Koch (612).....20 Wabash Ave., West End
R. A. MacDowell (613).....345 Fourth Ave.
William Maisch (616).....307 Fourth Ave.
J. F. McClurg (614).....312 Fourth Ave.
R. L. McKallip (615).....411 Seventh Ave.
Thomas C. McMahon (640).....731 Grant Bldg.
L. W. Monteverde (641).....427 Fourth Ave.
Albert A. Murrer (584).....614 Plaza Bldg.
Donnell D. Reed (708).....504 City-County Bldg.
S. L. Seemann (657).....341 Fourth Ave.
Frank T. Trohaugh (617).....514 Oliver Bldg.

Scranton
C. G. Chappell (376).....Bliss Davis Bldg.

Wilkes-Barre
C. A. Leighton (135).....Deposit & Savings Bk. Bldg.
Edward L. Lewith (227).....428 Miners Bk. Bldg.
L. D. Scranton (100).....147 N. Franklin St.

Williamsport
Fred B. Wetzel (721).....25 W. Third St.
Louis A. Wetzel (709).....442 William St.

RHODE ISLAND

Pawtucket
Leo V. Boyle (722).....44 Broad St.

Providence
Hal Forrester Coombs (172).....211 Waterman St.
Richard A. Hurley (513).....723 Hospital Tr. Bldg.

TENNESSEE

Memphis
Elbert A. Cheek (547)....801-6 Columbian Mutual Tower
George W. Person (320).....
.....Second Floor, Manhattan Bk. Bldg.
W. H. Prince (374).....1816 Poplar Ave.

Nashville
J. W. Denis (140).....535 Church St.
J. W. Graham (83).....930 Kirkwood Ave.

TEXAS

Amarillo
Robert Ricks (566).....Bivins Bldg.

Austin
Wilhelmine B. Sheffield (723).....207 W. Seventh St.

Beaumont
J. S. Edwards (444).....San Jacinto Bldg.

Corpus Christi
Jay E. Adams (626).....205 Guggenheim & Cohen Bldg.

Dallas
Henry S. Miller (277).....405 Southland Life Bldg.
Lawrence Miller (386).....2729 South Blvd.
John W. Pat Murphy (384).....1420 Commerce St.

Fort Worth
Meredith R. Carb (354).....510 First Nat. Bk. Bldg.

Houston
W. G. Burchfield (274).....803 Second Nat. Bk. Bldg.
L. A. Casey (353).....Esperson Bldg.
A. R. Foster (619).....1525 Marshall St.
Meredith H. James (681).....Esperson Bldg

San Antonio
Paul W. Adams (355).....Builders Exchange Bldg.
A. H. Cadwallader, Jr. (352)..920 Nix Professional Bldg.
Charles W. Cart (724).....307 E. Pecan St.
C. Ray Davis (618).....716 Travis Bldg.
Claris M. Elmore (356).....200 Betty Jean St.
Harold W. Keller (620).....714 Travis Bldg.
Reginald W. Patton (317).....621 Travis Bldg.

UTAH

Salt Lake City
Werner Kiepe (567).....139 S. Second St., E.

VIRGINIA

Newport News
Emanuel E. Falk (548).....117 26th St.

Richmond
John W. Bates (240).....723 E. Main St.
Henry S. Raab (260).....710 E. Main St.
J. Guthrie Smith (144).....329 Clovelly Rd.
Morton G. Thalhimer (221).....1013 E. Main St.

WASHINGTON

Bellingham
E. A. Wheeler (682).....1411 Commercial St.

Seattle
Charles P. Burnett (378).....14410 Third St., N. W.
Arthur E. Burr (576).....623 Second Ave.
Ralph H. Davis (577).....400 Skinner Bldg.
William A. Eastman (307).....414 University St.
R. C. Erskine (578).....2201 Northern Life Tower
Lloyd P. Hayworth (683).....200 17th Ave., N.
Ogden Johnson (658).....400 Skinner Bldg.
Walter G. McLean (346).....1108 Third Ave.
J. C. McQuigg (344).....1317 Boven Ave.
Vincent D. Miller (579).....337 Henry Bldg.
Ben J. Smith (343).....1222 Second Ave.
J. H. Sparkman (349).....1108 Third Ave.
Roy F. Taylor (659).....Seattle Tr. & Savings Bk.
Cecil S. Van Voris (369).....F.H.A., 1817 Exchange Bldg.
David T. Young (580).....511 Marion Bldg.

WEST VIRGINIA

Charleston
Charles Uhrig (79).....Box 1019

Clarksburg
Lyle B. Hornor (375).....Goff Bldg.

Wheeling
Harry C. Miller (725)....Rm. 2064, Board of Trade Bldg.

WISCONSIN

Madison
Stanley C. Hanks (642).....24 W. Mifflin St.
Paul E. Stark (643).....124 W. Mifflin St.

Milwaukee
Fritz W. Beck (581).....1708 N. 72nd St., Wauwatosa
Lloyd M. Boyce (621).....735 N. Water St.
K. Lee Hyder (185).....525 E. Michigan St.
Robert F. Marty (622).....709 N. 11th St.
Arnold P. VanLoghem (691).....235 W. Galena St.

Racine
Victor E. Johnson (684).....433 Wisconsin St.
Kenneth E. Sarles (710).....218 Fifth St.

ONTARIO, CANADA

London
Bert Weir (138).....156½ Dundas St.

Toronto
William Henry Bosley (623).....28 Adelaide St., W.
Cyril R. De Mara (12).....372 Bay St.
Frank McLaughlin (7).....34 King St., W.

The officers of the Institute announce with sincere regret the death of William S. Guilford, M.A.I., Oakland, California; admitted July 1, 1932; died January 29, 1939.

FEATURE ARTICLES IN THE LAST FOUR ISSUES OF *The* APPRAISAL JOURNAL

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